Canada's Venture Capital Landscape

May 2024

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Message from the President and Chief Executive Officer

Isabelle Hudon
President and Chief Executive Officer, BDC

BDC is pleased to present the 2024 edition of the Canada's Venture Capital Landscape report. To further support Canada's venture capital (VC) industry, this year, our efforts have been focused on delivering a report that is more comprehensive than ever before.

For the first time, we have compiled and analyzed regional data, allowing us to provide insights into VC activity across Canadian regions. Our deep dive into provincial activity spans the last five years and covers key indicators for the regions of Ontario, Quebec, British Columbia, the Prairies and Atlantic Canada.

Apart from this addition, our report still offers a thorough examination of the industry, combining internal and external data to provide a detailed overview of the state of Canada's VC landscape. Our analysis shows that although Canadian VC continued to demonstrate signs of maturation and steady growth when excluding recent outlier years, the ongoing reset experienced by the industry is starting to impact its performance and outlook.

"As an enabler, BDC has supported the evolution of the VC ecosystem for over a decade now and we will continue to do so across market cycles. Acting as a catalyst for growth, a strong and dynamic VC industry fosters an environment conducive to not only nurturing Canada's most innovative businesses but also scaling them into global champions."

Message from the President and Chief Executive Officer (cont.)

Against this backdrop, questions around eventual commitments from institutional investors in the asset class and future capital availability arise. While maturing, Canada's VC industry is at its inflection point, still calibrating its sustainable growth path. Confidence and sustained capital allocation in the asset class during this critical period will support its continued evolution. Throughout this period of reset, the industry's resiliency and progress over the last decade should not be forgotten.

As an enabler, BDC has supported the evolution of the VC ecosystem for over a decade now and we will continue to do so across market cycles. Acting as a catalyst for growth, a strong and dynamic VC industry fosters an environment conducive to not only nurturing Canada's most innovative businesses, but also scaling them into global champions.

Furthermore, integration of environmental, social and governance (ESG) standards and diversity, equity, inclusion, and accessibility (DEIA) initiatives remains important to fostering the growth of strong and sustainable businesses, and the economy.

As Canada's most active limited partner (LP) in the VC space, BDC undertakes an annual data collection exercise on DEI and ESG within its portfolio of general partners (GPs) and underlying portfolio companies. We report back findings to help identify and understand risks, but also support the Canadian VC and mid-market private equity (PE) industry improve over time. At the core of ESG integration lie people, transparency and collaboration, so we would like to thank our partners, portfolio GPs and companies for embarking on this journey with us. Through sustained efforts and time, we actively contribute to elevating our industry, making it more competitive and resilient.

All in all, Canada's maturing VC industry, its resiliency, as well as our entrepreneurs' ambitions and their growing commitment to sustainability, are intrinsically linked. At BDC, we firmly believe that by leveraging our capital-D, embracing greater risks and strategically aligning capital with innovation, we actively contribute to propelling entrepreneurs and our entire country toward long-term prosperity.

Executive summary

With interest rates reaching levels unseen since 2001, the Canadian VC community experienced a heightened sense of pessimism entering 2023. Last year's report described declining VC activity and GDP growth after a banner year in 2021. Understandably, with capital costs climbing, many market participants had a gloomy outlook for 2023.

Yet, our findings suggest that the anticipated worst-case scenario has not materialized. 2023 showcased both signs of resilience and fragility—some cautious optimism is warranted but must be tempered by persistent fundraising challenges and subdued returns. After a decade of growth, the market faced headwinds and experienced a reset over the last two years.

Despite our cost of capital cresting last year, Canadian VC-backed companies raised $6.9 billion in 2023.

Compared with global VC investment, Canadian VC experienced a slower decline in dollars invested.

Moreover, with interest rates expected to come down from the current rate of 5%, VC activity may stabilize in years ahead as the lag effect of comparatively lower cost of capital gets reflected in the ecosystem.

Though the information and communication technology (ICT) sector continues to account for the lion's share of VC investments, we are seeing a slight reallocation and increased investor interest in life sciences, and energy and clean technology (ECT) deals—a trend that is likely to persist, at least for ECT, as we collectively take action to reach Canada's net-zero emissions target by 2050.

41 VC-backed unicorns—companies with a value of more than $1 billion—were created over the last five years across Canada. Ontario generated the highest number of unicorns over that period, demonstrating the region's ability to grow and scale businesses. Ontario also led the way last year, with Quebec and British Columbia following not far behind.

The initial public offering (IPO) lull continued in 2023, with only one Canadian VC-backed company completing an IPO listing. On the other hand, mergers and acquisitions (M&A) reached record-high exit values. Although a few large deals drove the total exit value, even when excluding outlier deals, the overall median exit value increased. With interest cuts on the horizon, valuations may find a stable footing while M&A activity could potentially see an uptick.

An evolving market

First time and developing managers[1] continue to represent the lion share (82%) of total active general partners (GPs) cumulatively. However, there continues to be steady progression of GPs successfully raising subsequent funds, which underscores the increasing maturity of our ecosystem. The current macroeconomic backdrop is challenging for GPs actively fundraising, with many not achieving their ideal first close and final close targets, or not being able to raise altogether. In all cases, timelines to achieve fundraising milestones are significantly lengthened.

We also observe a decline in bridge financings, suggesting that companies in need of capital are returning to priced rounds. And while fundraising activity at the company level has slowed in comparison to 2021, the activity levels are still higher than during the pre-pandemic period (2015-19). Future fundraising will depend on, among other factors, whether valuations undergo further corrections, and whether the industry is able to maintain its double digits net internal rates of return (IRR).

[1] First time managers have closed fund I, developing managers have closed funds II and/or III. Taken together these are considered emerging managers.

Executive summary (cont.)

If net returns were to fall into the single digits, institutional investors would likely reallocate some of their investments to other asset classes, negatively impacting capital availability for GPs and companies alike.

10-year VC net returns remained in double digits last year. Some vintage cohorts were more affected by the market correction, but median distributed to paid-in capital (DPI) improved across all vintages in 2023, except for the 2020-22 cohort, which is still young.

When it comes to dry powder—the amount of committed, but unallocated capital a VC manager has on hand—we further enhanced our methodology in this report in an effort to increase precision. As a result, this year's results cannot be compared to last year's. In light of this, our calculations indicate that Canadian GPs hold an estimated $10.4 billion in dry powder. Furthermore, American investors currently hold a record $421 billion in dry powder[2], with 2% of it historically directed toward Canadian companies.

Overall, we believe the data reveals the possibility for slight optimism despite the turbulences of the past few years. However, lingering issues will no doubt continue to influence a sustainable growth rate we can expect for the asset class. In particular, as the industry looks to demonstrate enduring profitability, the bar for new investment will be raised. In light of this, companies and GPs that aren't meeting now-higher investor expectations will undoubtedly encounter difficulties.

Canadian GPs hold
$10.4 billion
in dry powder.

[2] Source: PitchBook-NVCA, data as of June 30, 2023

VC activity through a national and regional lens

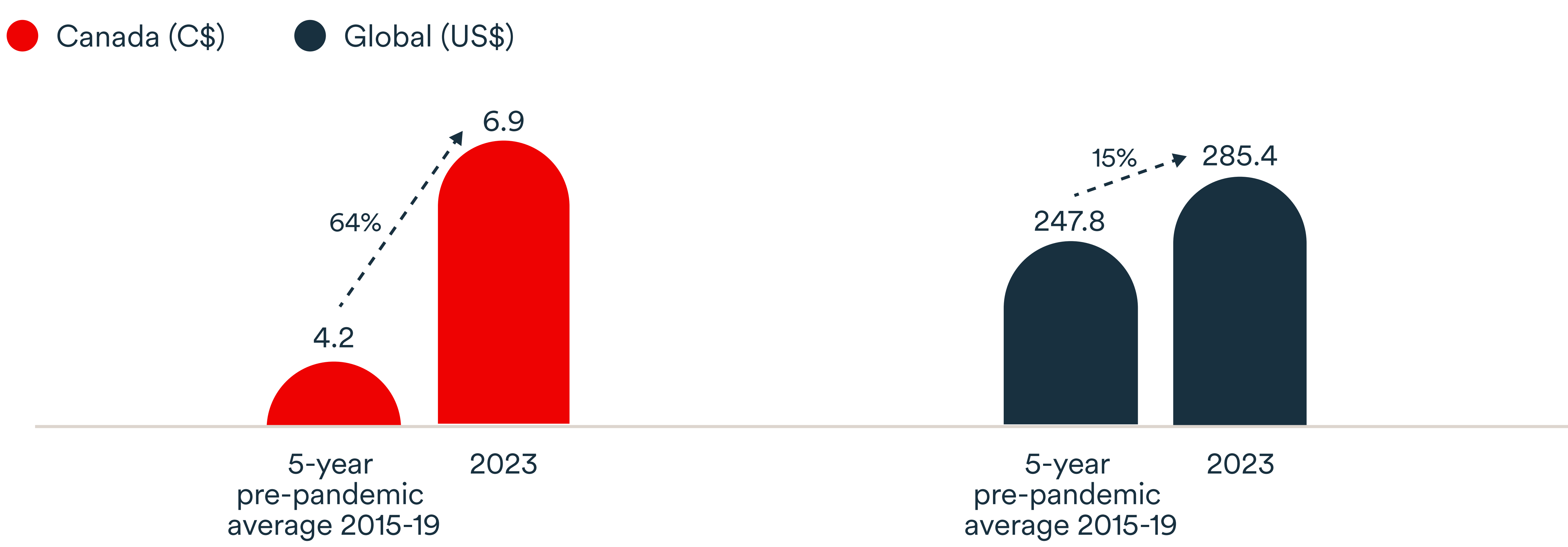
Canadian market remains active despite tough economic conditions

With $6.9 billion invested in Canada last year, marking a 34% drop from 2022 levels, VC activity continued its decline from the peak of 2021. It remains unclear whether the trajectory will continue its downward descent. As the industry struggles to adjust to the varying forces in the market, the question remains: Have we returned to a position which is sustainable? One aspect to consider is how the 2023 levels compare to the pre-pandemic era (2015-19). As can be observed from Figure 1, in 2023 Canadian VC investment increased 64% from the average of $4.2 billion during the 2015-19 era. Meanwhile global VC investment saw an increase of just 15% in comparison to the same period.

Furthermore, the number of deals that closed last year (660) was 25% higher than the 5-year average for the 2015-19 period. Overall, these numbers underscore a persistent interest by investors and an ecosystem that has remained active despite a challenging economic environment.

As the industry struggles to adjust to the varying forces in the market, the question remains: Have we returned to a position which is sustainable?

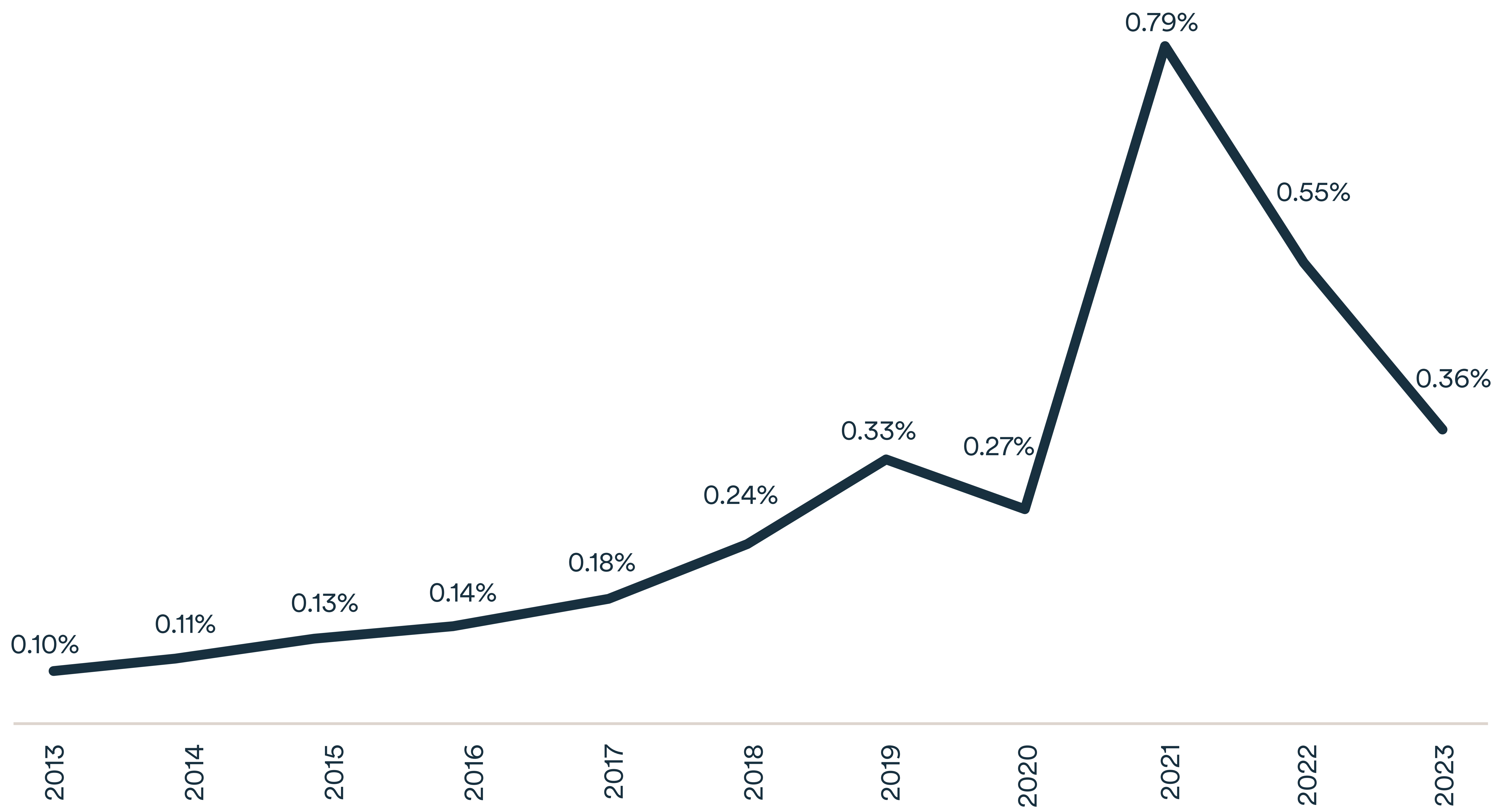
Figure 1: Canadian versus global VC investment growth from the pre-pandemic period to 2023 ($ billions)



Source: CVCA, Crunchbase; BDC analysis.

As seen in Figure 2, Canadian VC investments have continued to decline as a share of GDP since the peak of 2021, however the 2023 level was still higher than what it was in 2019 and earlier.

Figure 2: VC investments as share of GDP in Canada

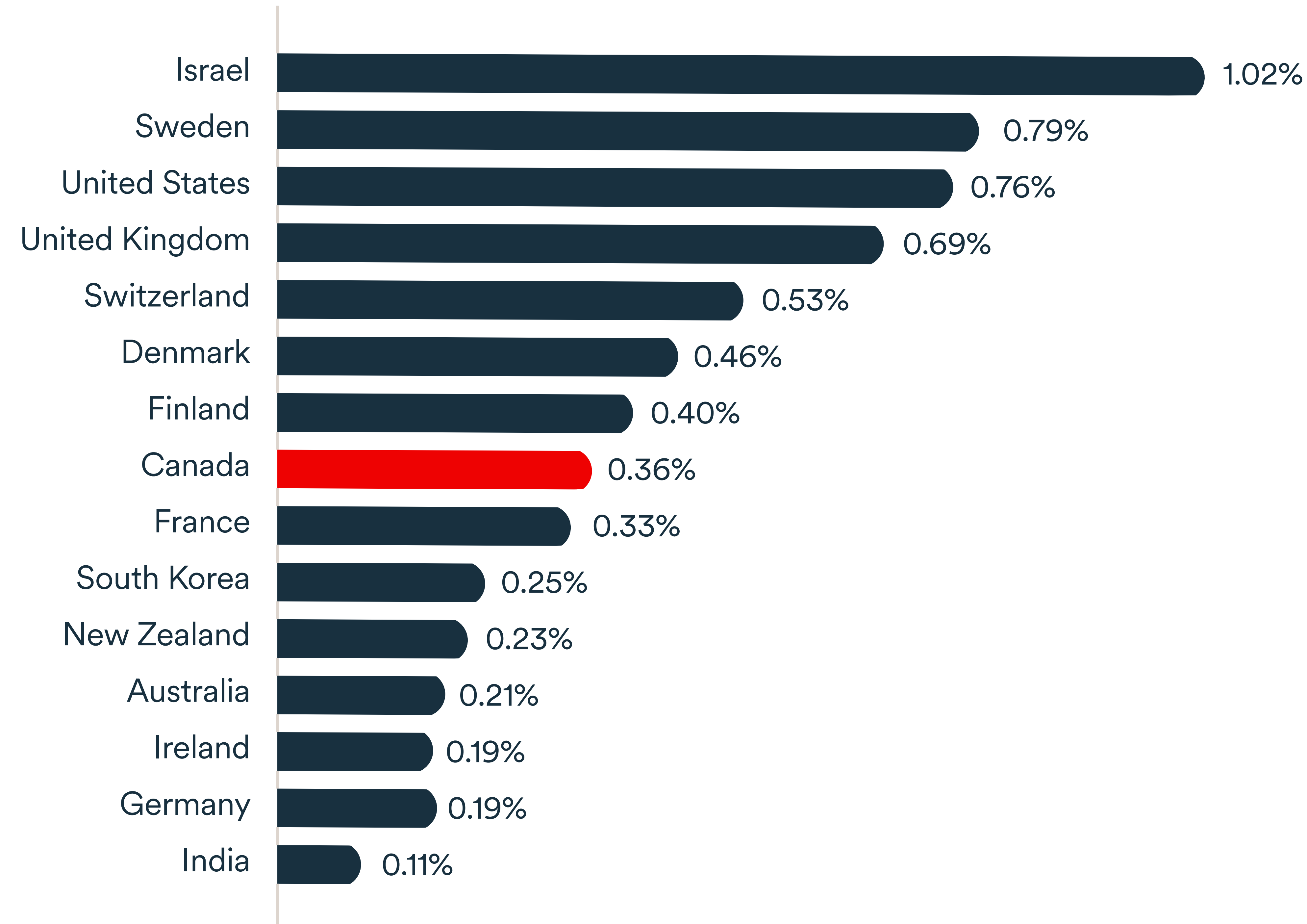


Source: PitchBook, OECD, BDC anaysis

Moreover, as a percentage of GDP, VC investments declined across OECD countries, with Canada landing in the middle of the pack (Figure 3).

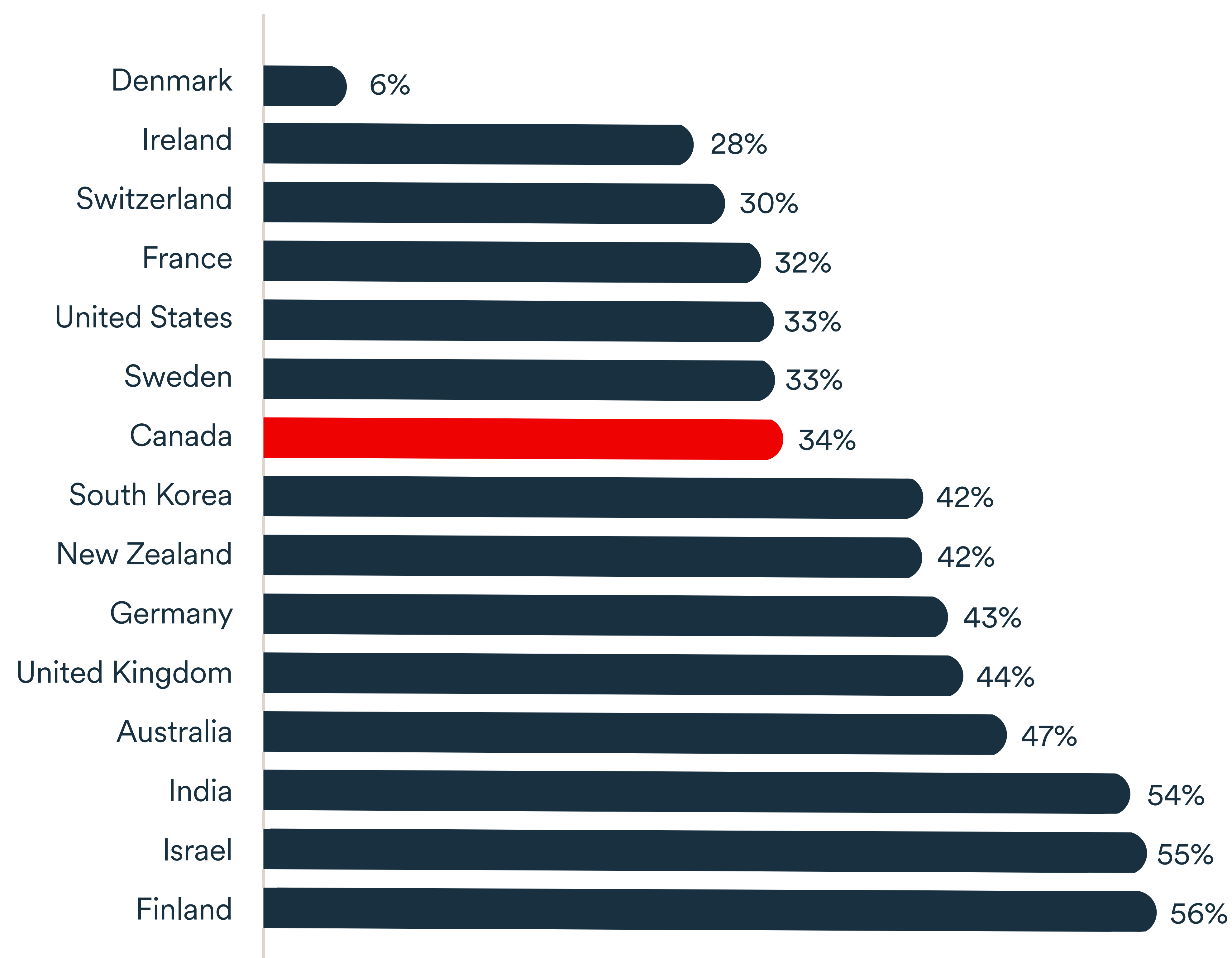
Canadian VC investment as a share of GDP declined to 0.36% in 2023. A 34% contraction from 2022 levels, which was closely in line with the contraction witnessed in the U.S. (Figure 4).

Figure 3: VC investments as a share of GDP in the OECD



Source: PitchBook, OECD, BDC analysis

Figure 4: Decline in VC investments as a share of GDP, 2022 to 2023



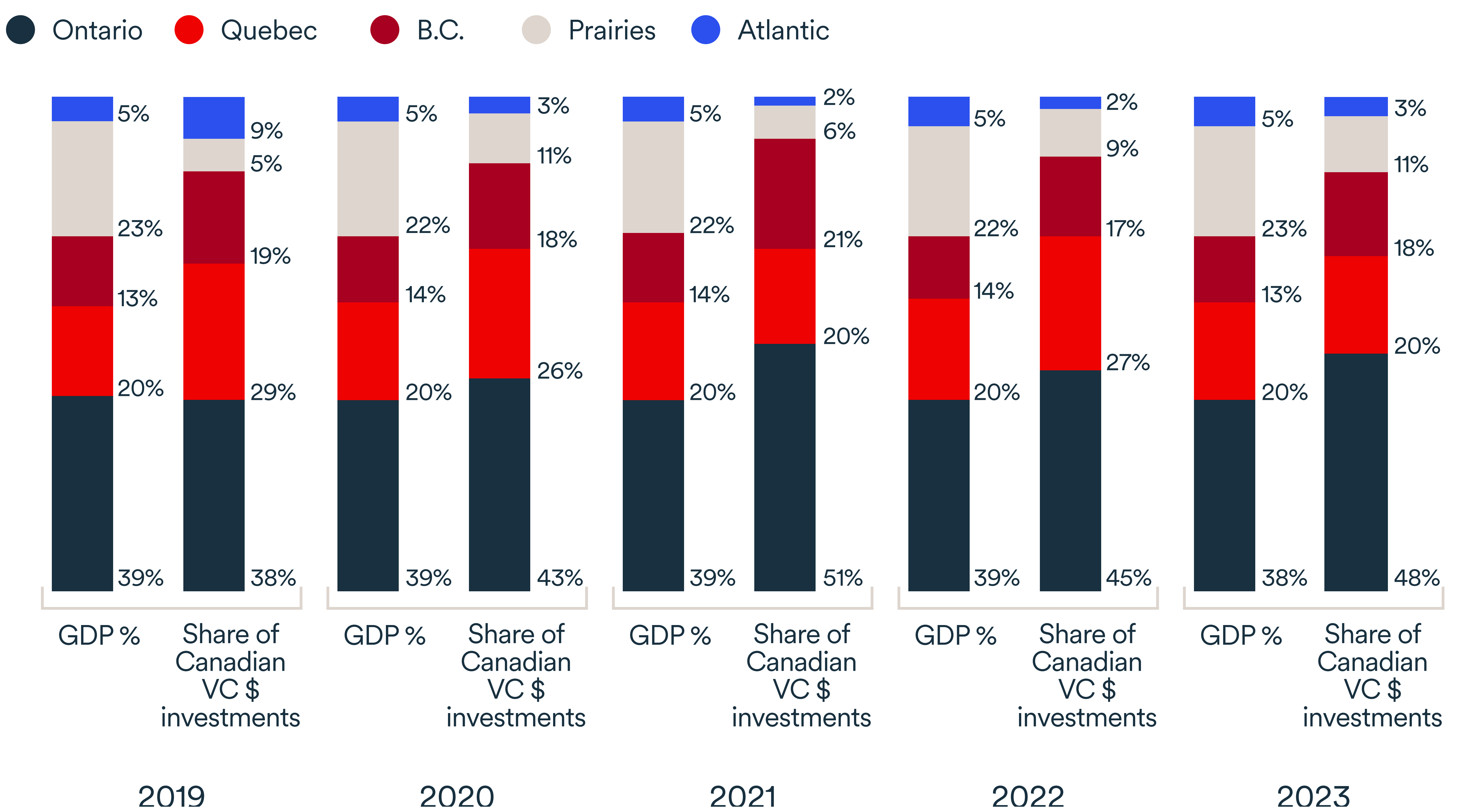
Source: PitchBook, OECD, BDC analysis
Note: To facilitate standardized comparison across countries, we used PitchBook VC activity data for all the countries included in this analysis.

Regional VC activity remains disparate across the country

It is imperative to understand the regional VC activity in Canada and to identify growing opportunities and areas of improvement. To that end, we have introduced new regional analysis this year and presented them in the following sections. We segmented the analysis across five regions that exhibited activity: Ontario, Quebec, British Columbia, the Prairies and the Atlantic. We analyzed each region's VC activity and compared it to that region's relative contribution to the Canadian GDP, from both a current and historical perspective (Figure 5). Due to the lack of data available for the Yukon, the Northwest Territories and Nunavut, we could not include these regions in this year's analysis.

Regional VC activity may not always align with that region's relative contribution to Canadian GDP. For example, we note that Ontario and British Columbia's respective share of Canadian VC investments in 2023 significantly exceeded their share of GDP in Canada. The largest deviation in 2023 was in Ontario—the province's VC investments represented 48% of total Canadian VC investments, while the region's economic output represented only 38% of Canada's GDP.

Figure 5: Regional VC investment relative to economic size within Canada



Sources: OECD, CVCA, BDC Analysis

Provinces in the Prairies have consistently attracted less VC funding than their relative size in the Canadian economy. However, the region's share of VC investments has grown in recent years—the second biggest increase among the regions since 2019, after Ontario. This increase can largely be attributed to Alberta and its strong ECT sector. Over the last five years, the Prairies has had the highest average relative contribution to the ECT sector after British Columbia and the Atlantic provinces.

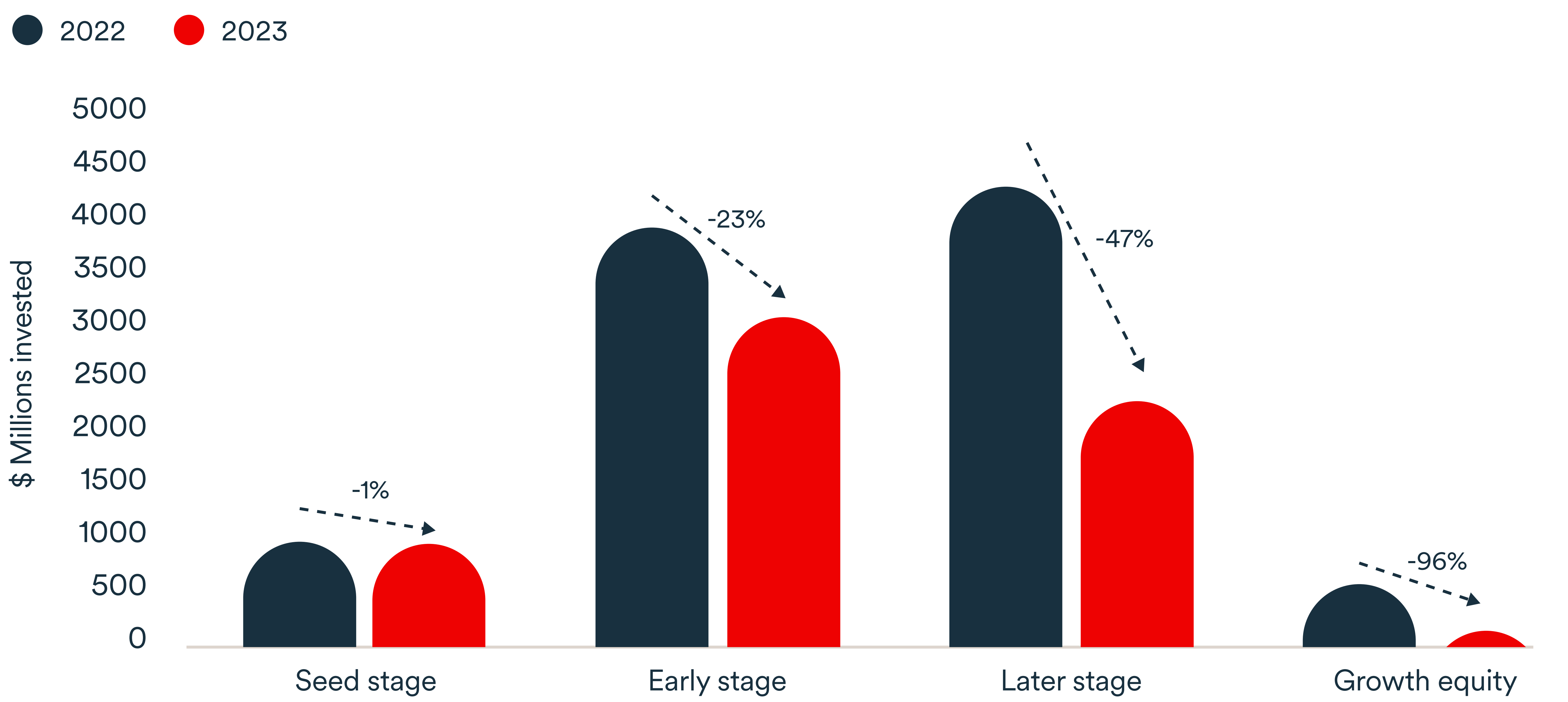
Meanwhile, the Atlantic provinces' share of VC investments have been trailing their economic size consistently, with the exception of 2019, but unlike the Prairies, no significant uptick in regional investment can yet be seen.

VC activity is shifting by stage and sector

In 2023, VC investment activity in Canada declined across all stages (Figures 6 and 7). Notably, the capital invested into late-stage companies was almost cut in half last year compared to 2022. Meanwhile, the number of deals only decreased by 19%, implying smaller cheque sizes.

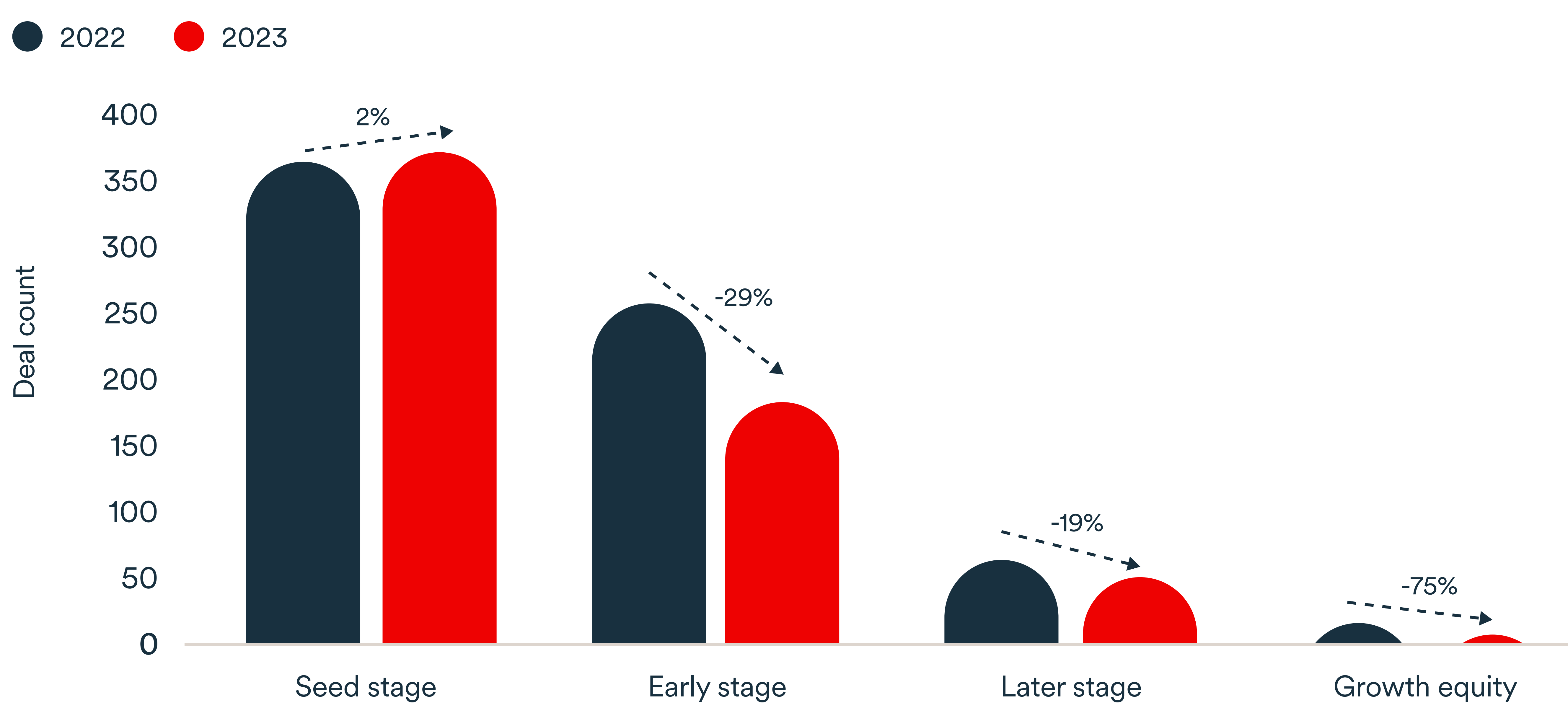
Early-stage investment rounds saw a smaller decline in comparison to later and growth stages. The seed stage maintained its resilience partially fueled by existing funds opportunistically migrating to this space and considering opportunities in earlier stages. However, if there is a sustained dearth in capital availability at the late stages, companies that are currently funded at the seed stage will find it challenging to scale should that funding gap persists.

Figure 6: VC investment, by stage



Source: CVCA, BDC analysis

Figure 7: VC deal count, by stage

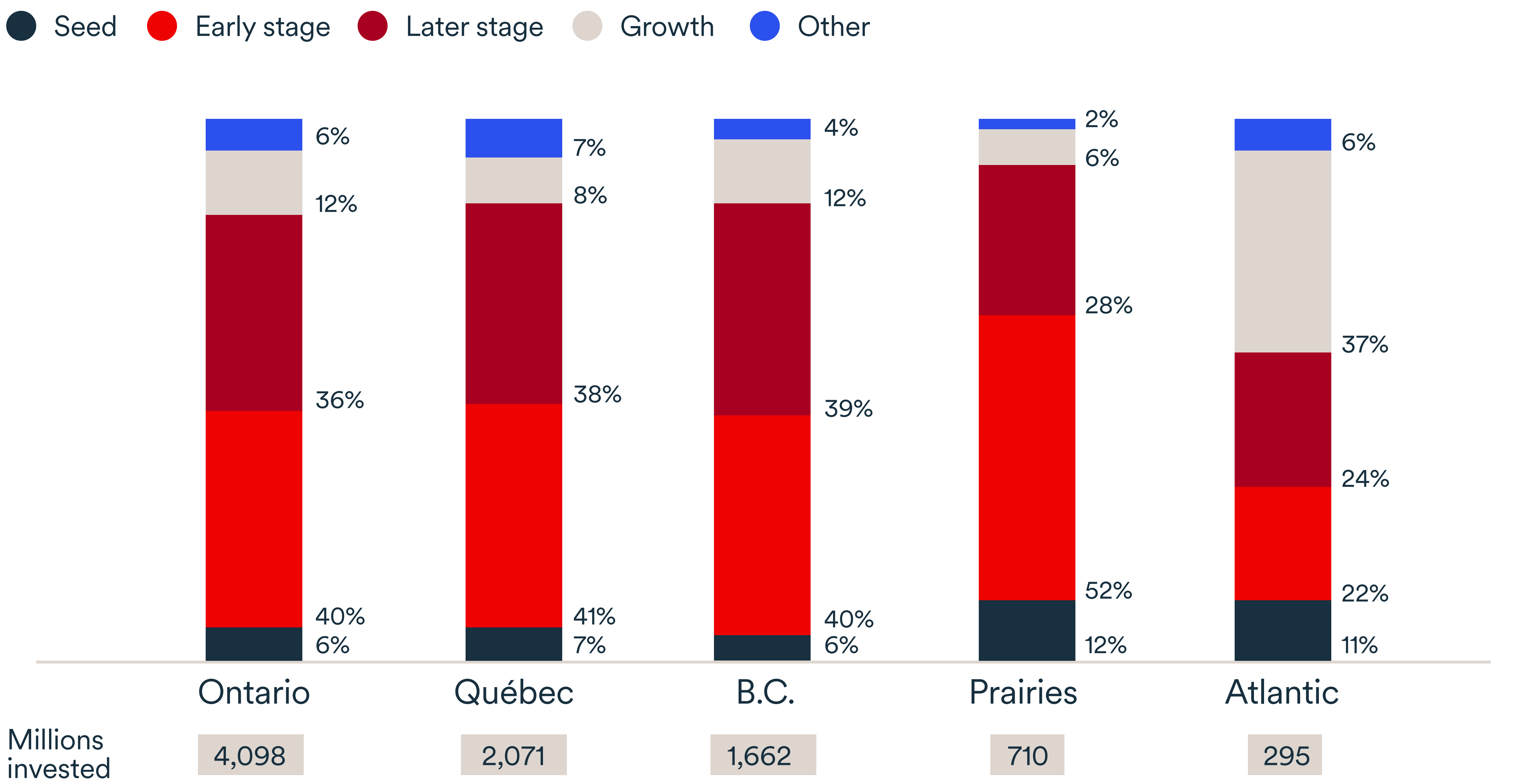


Source: CVCA, BDC analysis

Interesting trends can be found when looking at capital allocation by stage across regions. Looking at 5-year average VC investments (Figure 8), seed stage companies in the Prairies and the Atlantic receive about 11%-12% of regional investments. That is about double the share in Quebec, Ontario and British Columbia. In addition, the latter three provinces share similar distribution of investments across stages, whereas the Prairies and the Atlantic regions are characterized by emphasis on earlier or later stage investments.

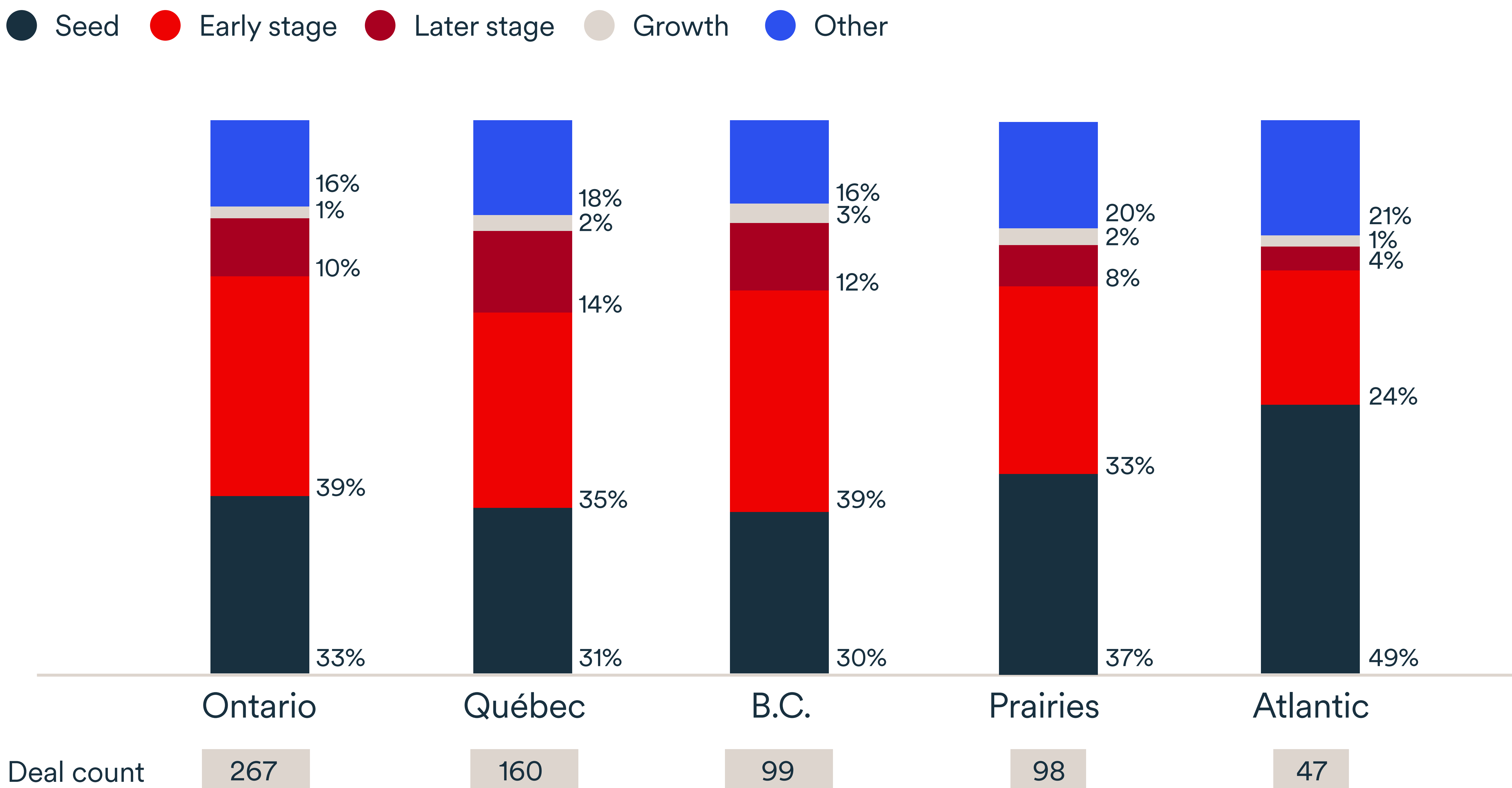
When we consider the deal counts (Figure 9), it becomes clear that a lot of investment dollars were concentrated in a limited number of companies in the Atlantic region. Furthermore, there is comparatively less late and growth stage investment in the Prairies.

Figure 8: Regional VC investments (5-year average), by stage



Source: CVCA, BDC analysis

Figure 9: Regional VC deal count (5-year average), by stage

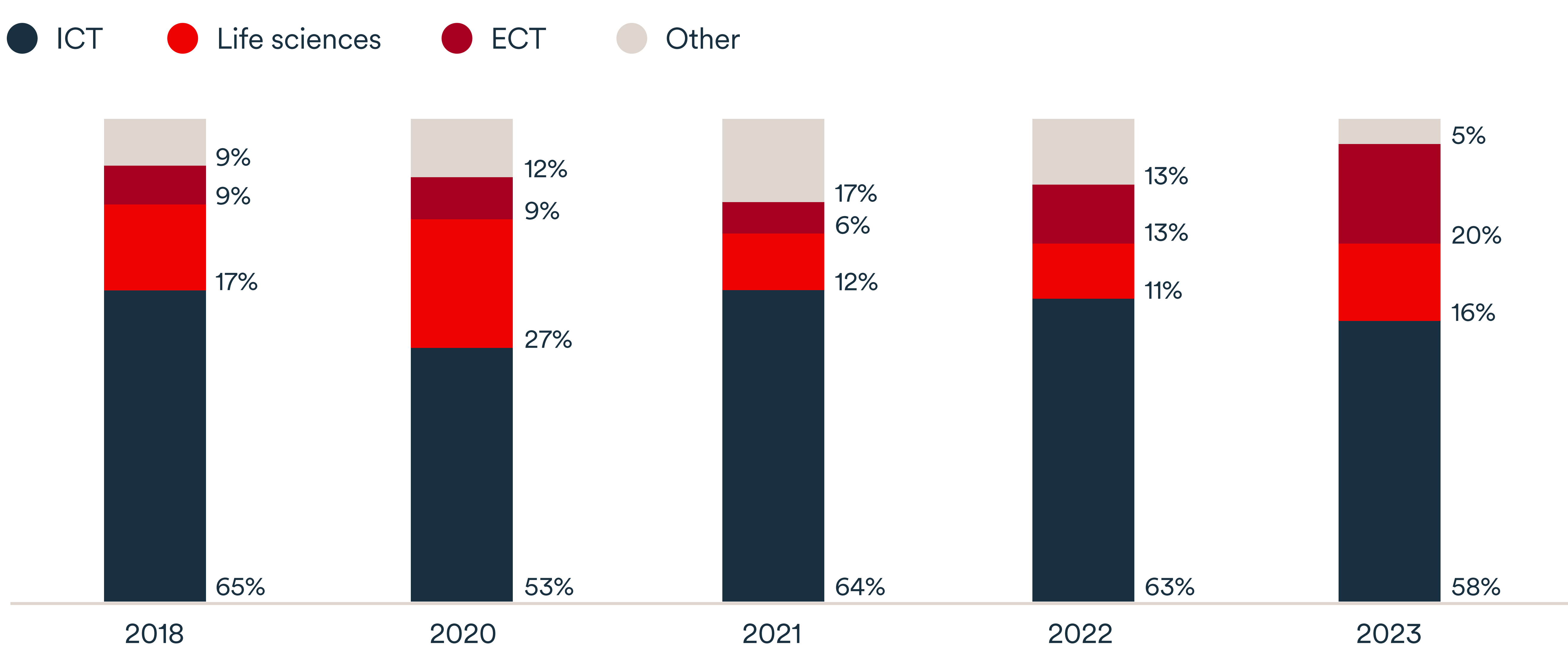


Source: CVCA, BDC analysis
Note: The data from 2021–23 for the "other" category includes "pre-seed" investments.

From a national lens, VC activity shifted slightly across sectors last year, although ICT remains the dominant sector (Figure 10). There was a decline in the proportion of dollars invested in ICT, while the ECT and life sciences sectors picked up steam. The life sciences and ECT sectors made up 16% and 20% of total dollars invested in 2023, compared to 11% and 13% in 2022, respectively.

ICT was partially fueled by the market's strong interest in AI-related investments, supported by the fact that Canada ranks third in the G7 for total funding per capita raised for AI companies, with more than 670 Canadian AI start-ups and 30 Canadian generative AI companies receiving at least one investment deal valued at more than US$1 million since 2019.[3] We expect that the prevalence of AI and its adoption by various industries will fuel the growth of all sectors over the coming years.

Figure 10: VC investment, by sector



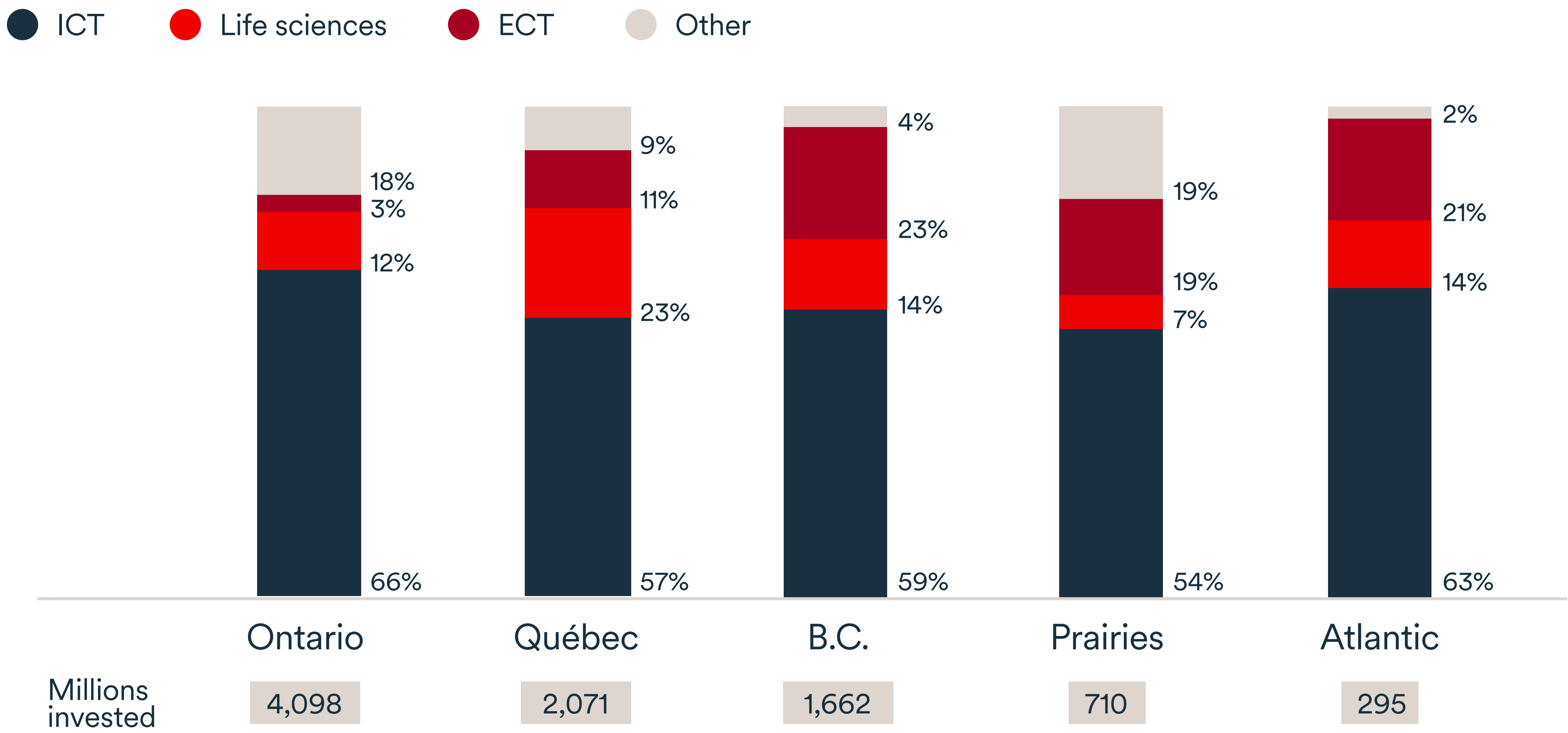
Source: CVCA, BDC analysis
Note: CVCA refers to the cleantech sector, whereas we refer to this sector as the energy and clean technology sector, which includes agribusiness companies.

[3] Prime Minister of Canada, Justin Trudeau, Securing Canada's AI Advantage, April 7, 2024.

From a regional lens (Figures 11 and 12), since 2019, the ICT sector has accounted for more than half of all dollars invested across the provinces, making it the leading sector throughout Canada. The sector in second place for investment, however, varied by region. The ECT sector's share of investment was lower in Ontario, at 3%, than elsewhere in Canada.

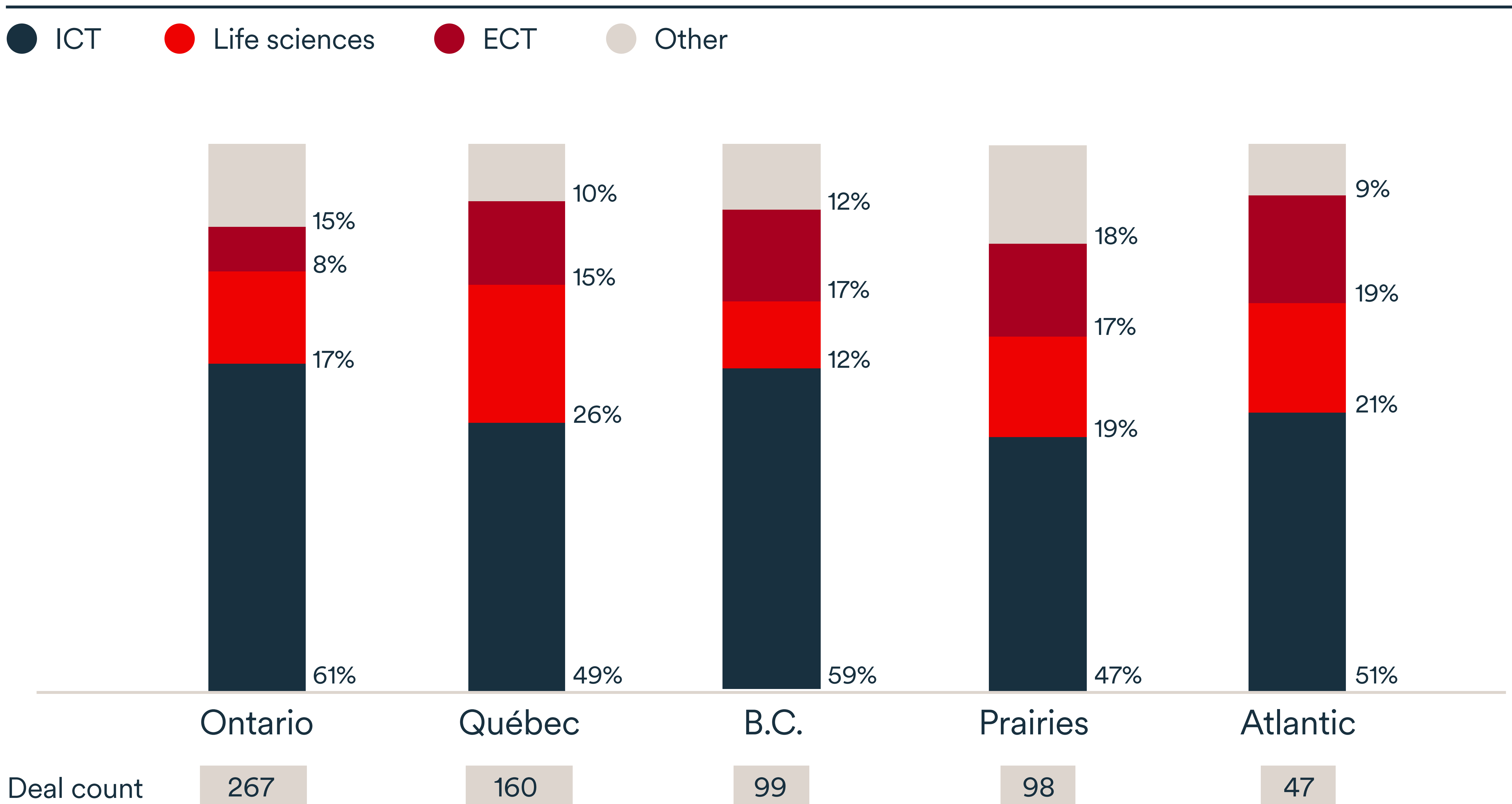
Meanwhile, life science represented 23% of investments in Quebec, the highest proportion for this sector across all regions. The ICT sector continued to have a strong foothold in Ontario, but there was a decline in the proportion of dollars invested in ICT in Quebec, British Columbia and the Atlantic provinces.

Figure 11: Regional VC investment (5-year average), by sector



Source: CVCA, BDC analysis

Figure 12: Regional VC deal count (5-year average), by sector



Source: CVCA, BDC analysis

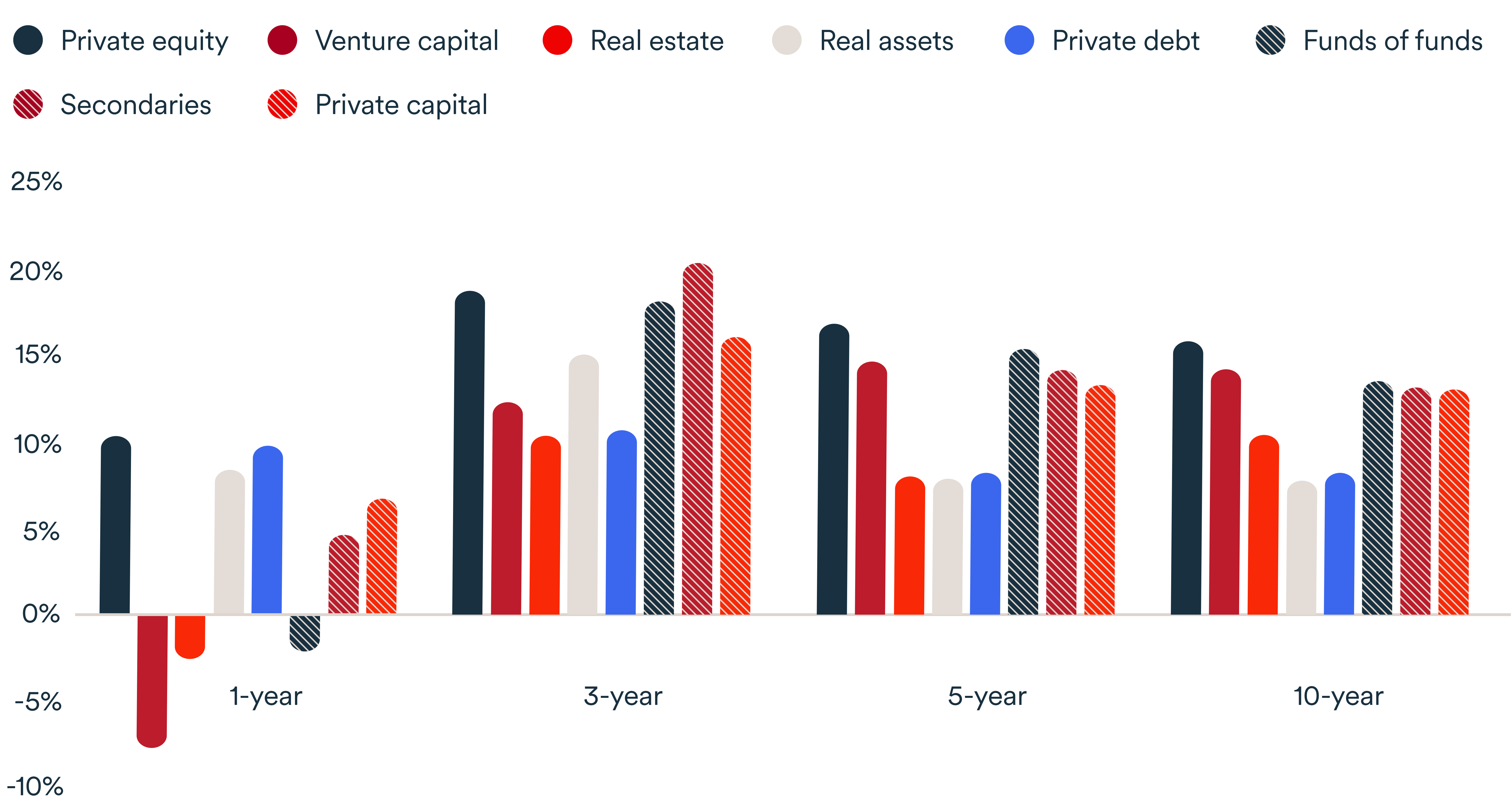
VC short-term performance strained; long-term double-digit returns maintained

Long-term global VC performance remained strong

As can be observed from Figure 13, on a global scale, VC continues to demonstrate strong long-term performance, with 5-year and 10-year IRRs at 15% and 14% respectively. However, 1-year VC IRR had negative returns, largely influenced by a valuation correction following the 2021 bubble.

This decline has been driven by several factors, including an increase in down rounds and proactive adjustments by GPs of company valuations based on fundamental metrics and market comparables. Consequently, the 1-year IRR for venture capital remained the lowest among private capital asset classes in 2023.

Figure 13: Global VC returns compared to other private capital asset classes



Source: PitchBook, data as of September 30, 2023

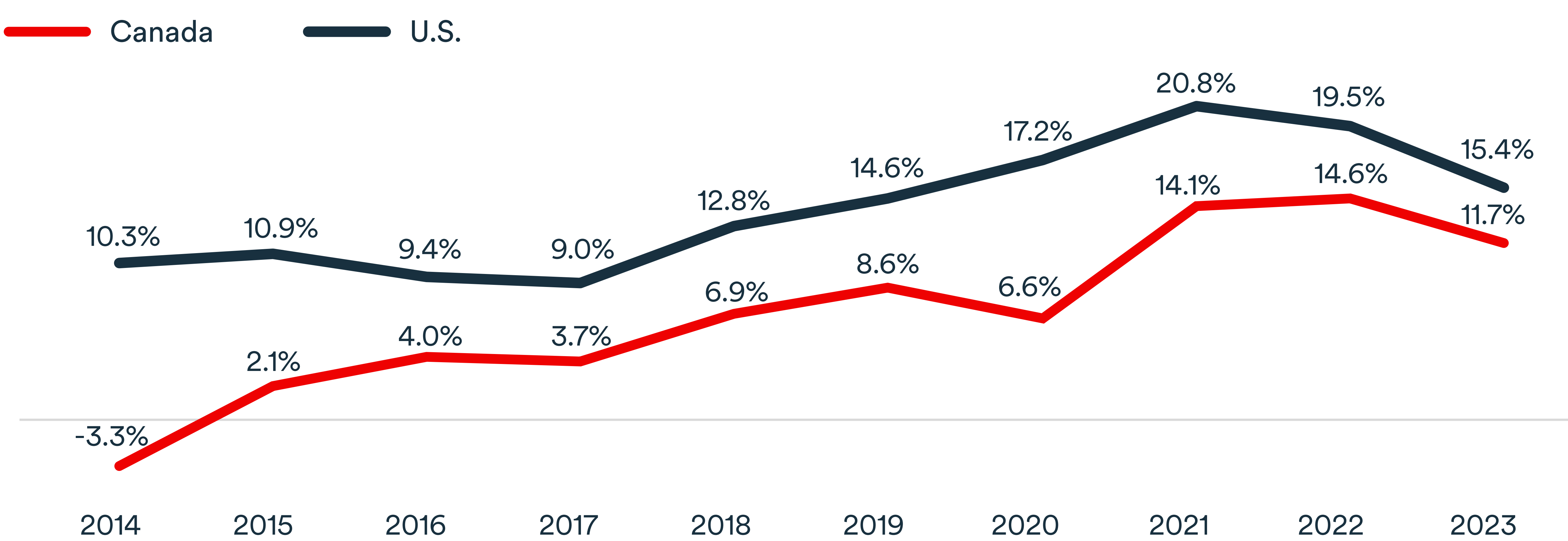
To evaluate VC performance in Canada, we created a proxy using 68 unique GPs from the BDC portfolio. As Canada's most active VC investor, BDC Capital's portfolio is diversified across vintages, stages and sectors. It therefore serves as a reasonable benchmark.

A persistent yet narrowing Canada-U.S. performance gap

Not unlike global VC returns highlighted above, Canadian 1-year performance was negative at -11.2%, however the 5-year and 10-year IRRs remained in the double digits at 11.5% and 11.7%, respectively. Should annual returns continue to drag for another year, we believe that Canada's 5-year and 10-year returns are likely to fall to single digits.

The Canadian VC 10-year IRR decreased to 11.7% last year (Figure 14), a decline mirroring the trend observed in the U.S. We note that the contraction in Canada was less severe at 290 basis points in comparison to the U.S., which saw a decline of 410 basis points. Although the gap in VC performance between the U.S. and Canada was still not closed in 2023, it has shrunk compared to the 5-year average.

Figure 14: 10-year VC net return (IRR) in Canada and the U.S.



Source: Cambridge Associates, U.S. VC benchmark preliminary data as of December 2023; BDC Capital fund investment data for VC funds headquartered in Canada and foreign-based funds with significant Canadian investment exposure, as of December 2023.

Disclaimer: BDC funds data as reported in the BDC financial statements serves as a proxy for Canada's VC performance. This data may understate the reported performance of invested funds due to BDC's more conservative valuation policy.

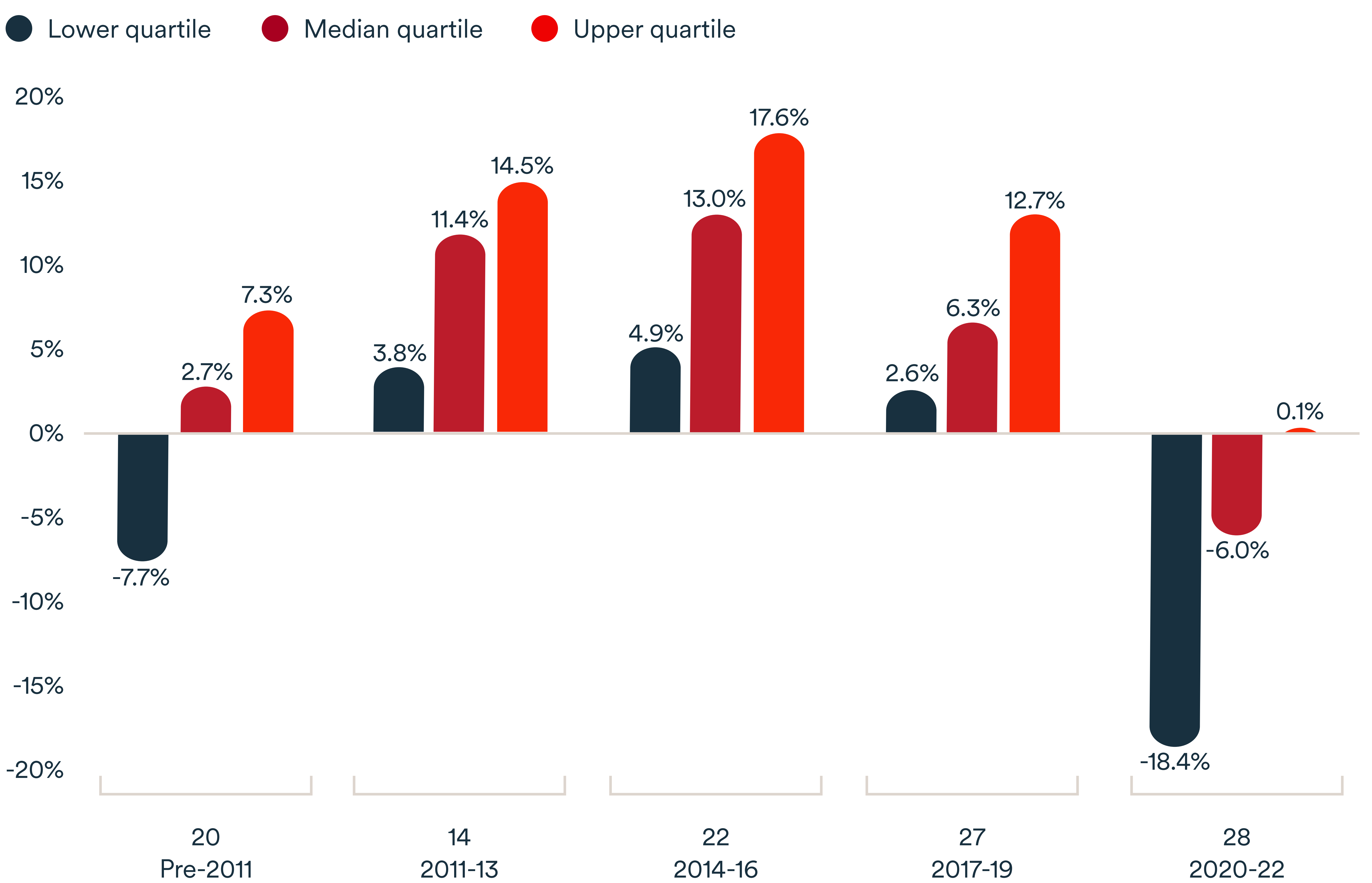
Note: BDC reviewed its methodology on classification of vintages to better align it with market practices, which may prevent comparing this year's data with those in previous reports.

We analyzed the distribution of three performance metrics across vintages: IRR, total value to paid-in capital (TVPI) and distributed to paid-in capital (DPI)[4]. However, we opted to exclude the 2023 cohort from our analysis, as these funds are too young to present any meaningful performance numbers.

This deep dive in Canadian VC performance across vintages reveals that, in line with general market conditions that deteriorated in 2023, the top quartile IRR decreased across all cohorts by an average of 370 basis points excluding the 2020-2022 vintage, which saw a larger decline as of December 31, 2023 (Figure 15).

This year's analysis found that managers that raised capital during the 2014-16 vintage delivered the best IRRs. However, with regard to TVPI and DPI, managers that raised during in the 2011-13 period have continued to provide robust returns.

Figure 15: IRR across vintages



Source: BDC Capital fund investment data for VC funds headquartered in Canada and foreign-based funds with significant Canadian investment exposure, as of December 2023. Number of funds in each vintage cohort is displayed in the graph just above the vintage grouping.

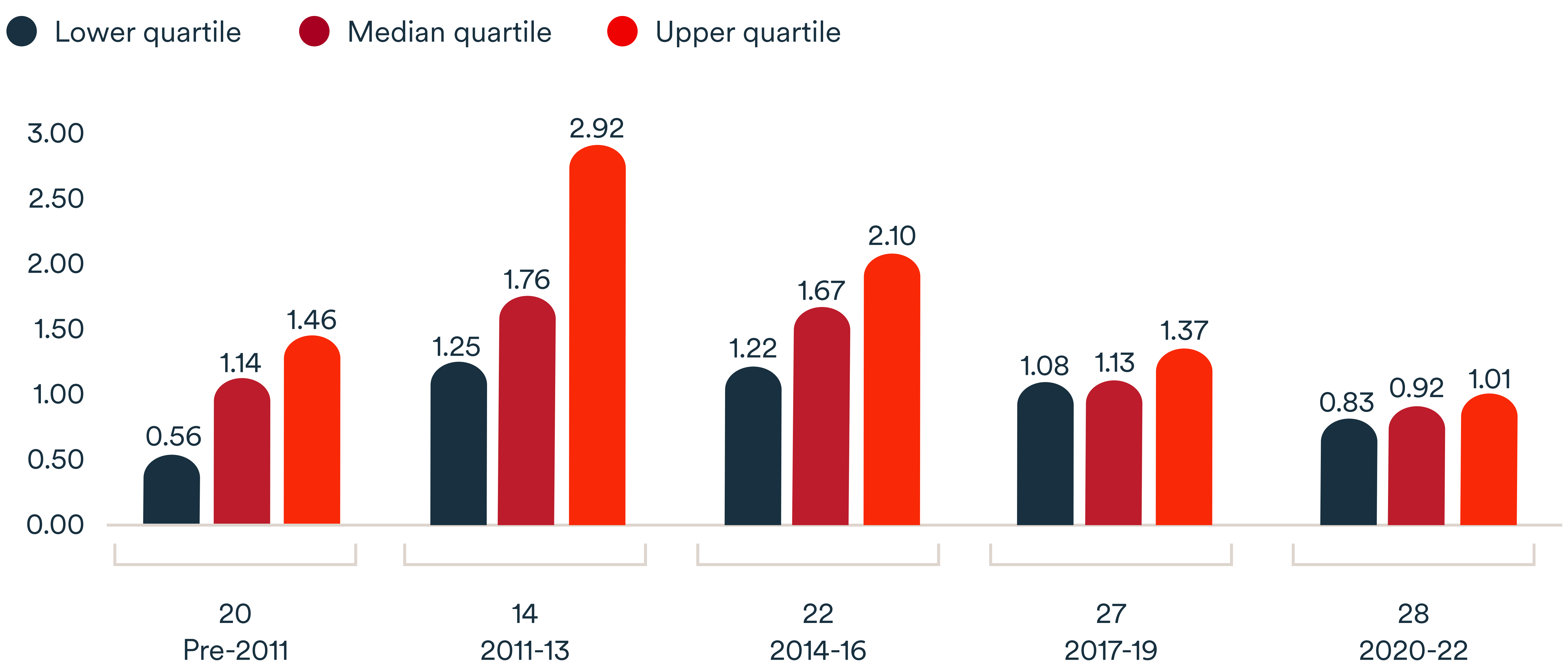
Disclaimer: BDC Funds data as reported in the BDC financial statements serves as a proxy for Canada's VC performance. This data may understate the reported performance of invested funds due to BDC's more conservative valuation policy.

Note: BDC updated its methodology on classification of vintages to better align it with market practices, which may prevent comparing this year's data with those in previous reports.

[4] TVPI includes the initial capital investment made by LPs plus the total value of all distributions to date. DPI is the ratio of money distributed to LPs relative to contributions.

The 2017-19 vintage cohort in our portfolio was most significantly affected by the market valuation correction. This cohort's TVPI is largely attributed to unrealized fair values, which experienced downward pressures in 2023. Within this same cohort, the top quartile TVPI decreased to 1.37, marking a 21% decrease compared to 2022. TVPI impact was not as significant for the 2020-22 cohort because these younger funds are still holding some of their investments at cost (Figure 16).

Figure 16: TVPI across vintages



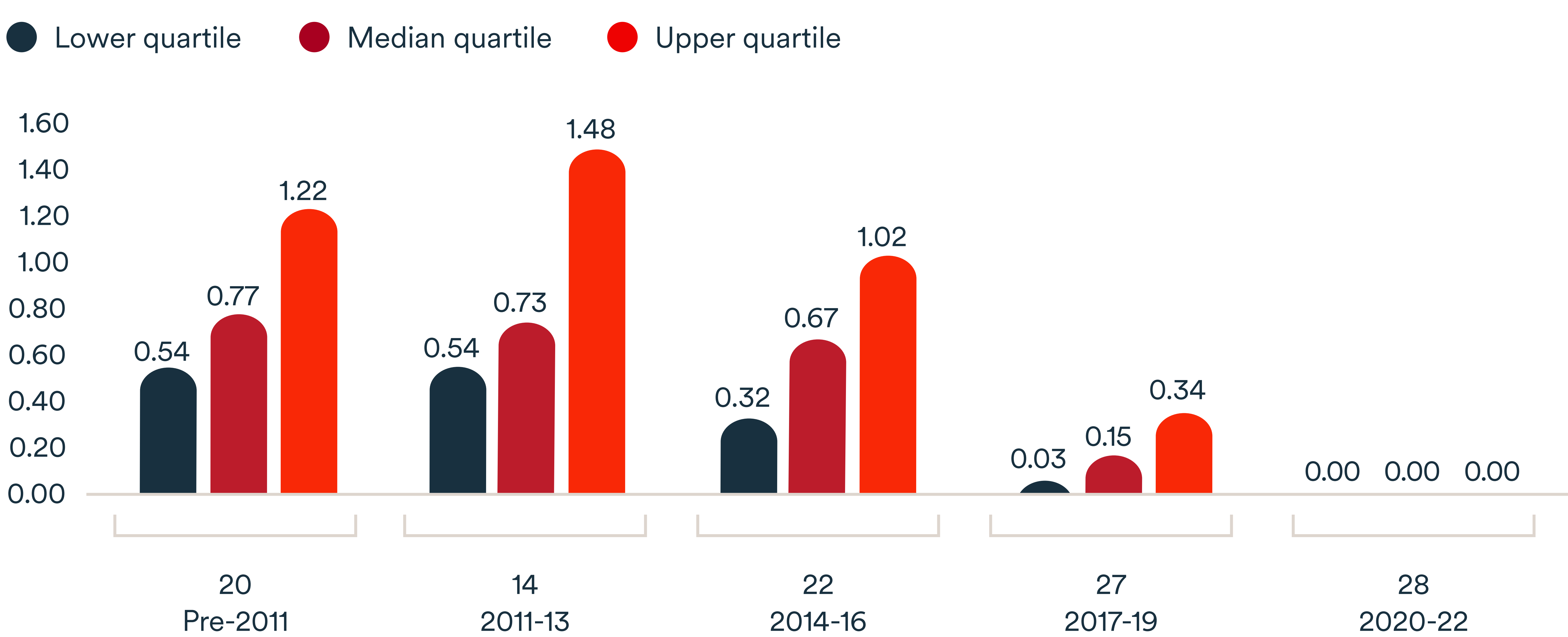
Source: BDC Capital fund investment data for VC funds headquartered in Canada and foreign-based funds with significant Canadian investment exposure, as of December 2023. Number of funds in each vintage cohort is displayed in the graph just above the vintage grouping.

Disclaimer: BDC funds data as reported in the BDC financial statements serves as a proxy for Canada's VC performance. This data may understate the reported performance of invested funds due to BDC's more conservative valuation policy.

Note: BDC reviewed its methodology on the classification of vintages to better align with market practices. This may prevent comparing this year's data with those in previous reports.

Median DPIs improved across vintages in 2023, except for the 2020-22 cohort, which is still young. This demonstrates that despite a challenging exit environment, at least a few Canadian GPs managed to return capital to their limited partners (LPs) (Figure 17).

Figure 17: DPI across vintages



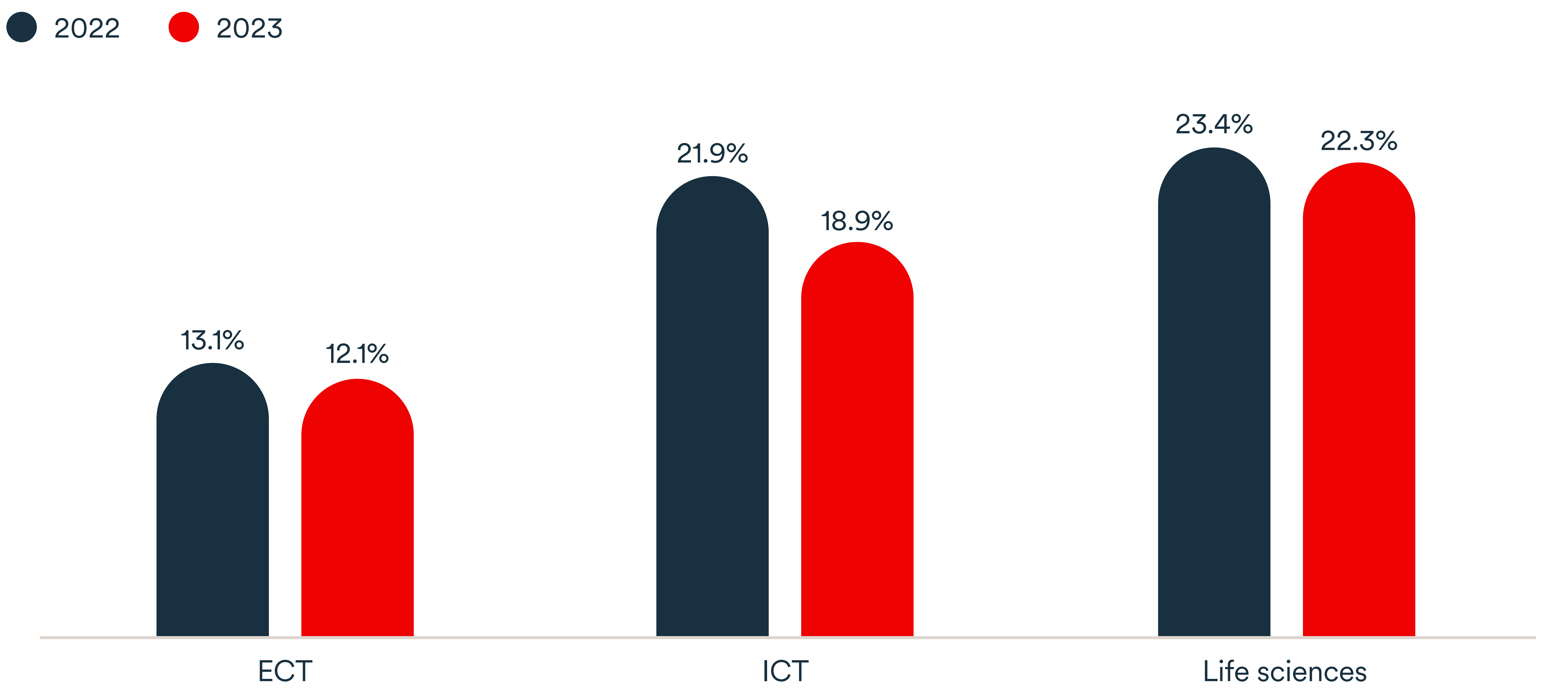
Source: BDC Capital fund investment data for VC funds headquartered in Canada and foreign-based funds with significant Canadian investment exposure, as of December 2023. Returns are net to BDC as reported in the financial statements. Number of funds in each vintage cohort is displayed in the graph just above the periods fund vintage cohorts grouping.

Note: BDC reviewed its methodology on classification of vintages to better align with market practices, which may prevent comparing this year's data with those in previous reports.

Magnitude of 10-year IRR contraction smaller in ECT and life sciences compared to ICT

Compared to 2022, 10-year performance declined in the ICT, ECT and life sciences sectors, but the contraction was sharper in the ICT space with a 300 basis points decline (Figure 18). The ECT and life sciences sectors showed somewhat more resiliency with a contraction of 100 and 110 basis points, respectively. However, over the time horizon, life sciences sector returns continue to outperform ECT and ICT, despite being relatively underfunded.

Figure 18: 10-year gross IRR by sector in Canada



Source: BDC data, as of December 31, 2022, and December 31, 2023. BDC direct and underlying companies are used as a proxy for sector performance.

Bridge financing tapering off; higher uptick in down rounds

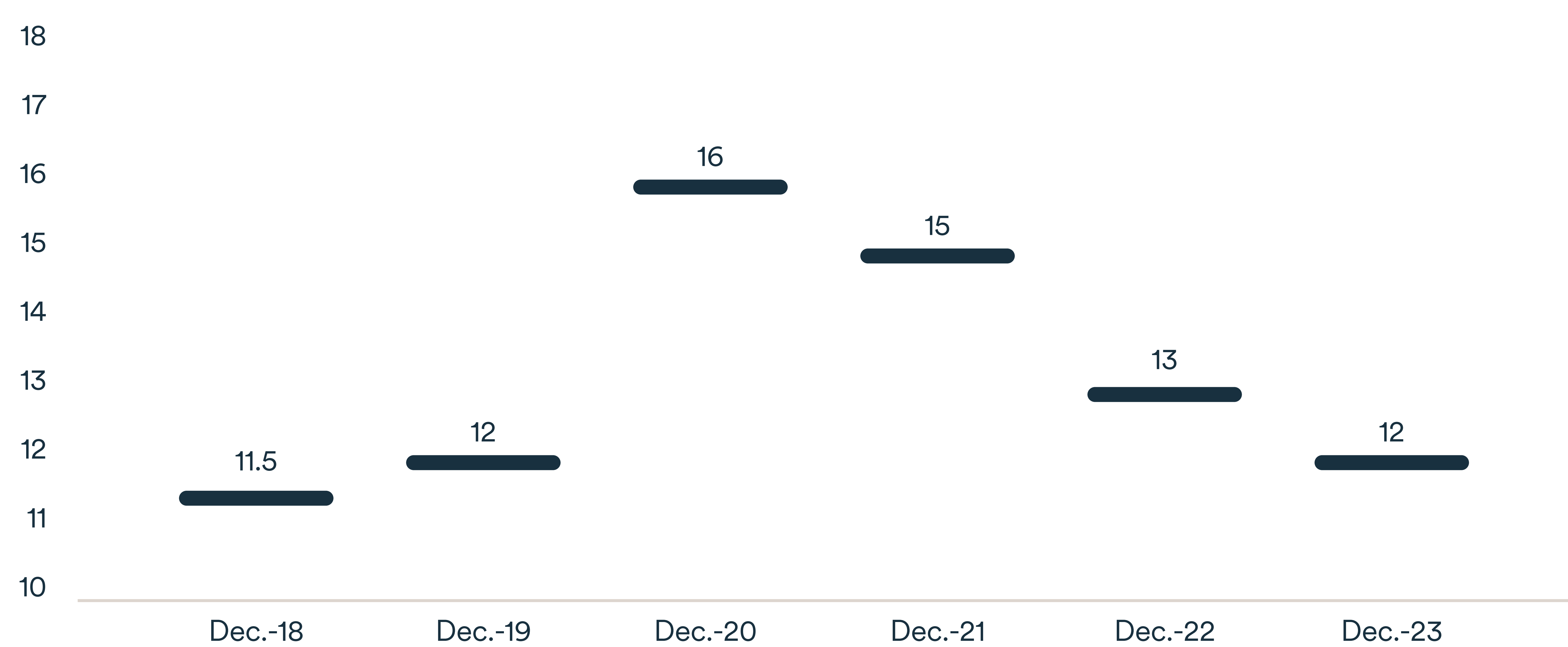
Cash runways getting shorter

The median cash runway of companies in BDC's direct portfolio, calculated in months, peaked at 16 months of runway in December 2020 (Figure 19), when the fundraising environment became more favourable to start-ups. At that point in time, larger fundraising rounds at higher valuations had become the norm. Following this peak, median cash runways gradually reverted to a mean of around 12 months.

This trend was observed across seed and early-stage companies. However, despite a contraction in investment activity, later-stage companies still managed to maintain longer runways of 18 months or more. This could be attributed to relatively more aggressive cost-cutting measures implemented in the later stages, as evidenced by a sample of late-stage companies within the BDC's direct portfolio.

Following this peak, median cash runways gradually reverted to a mean of around 12 months.

Figure 19: Median cash runways of BDC direct portfolio companies

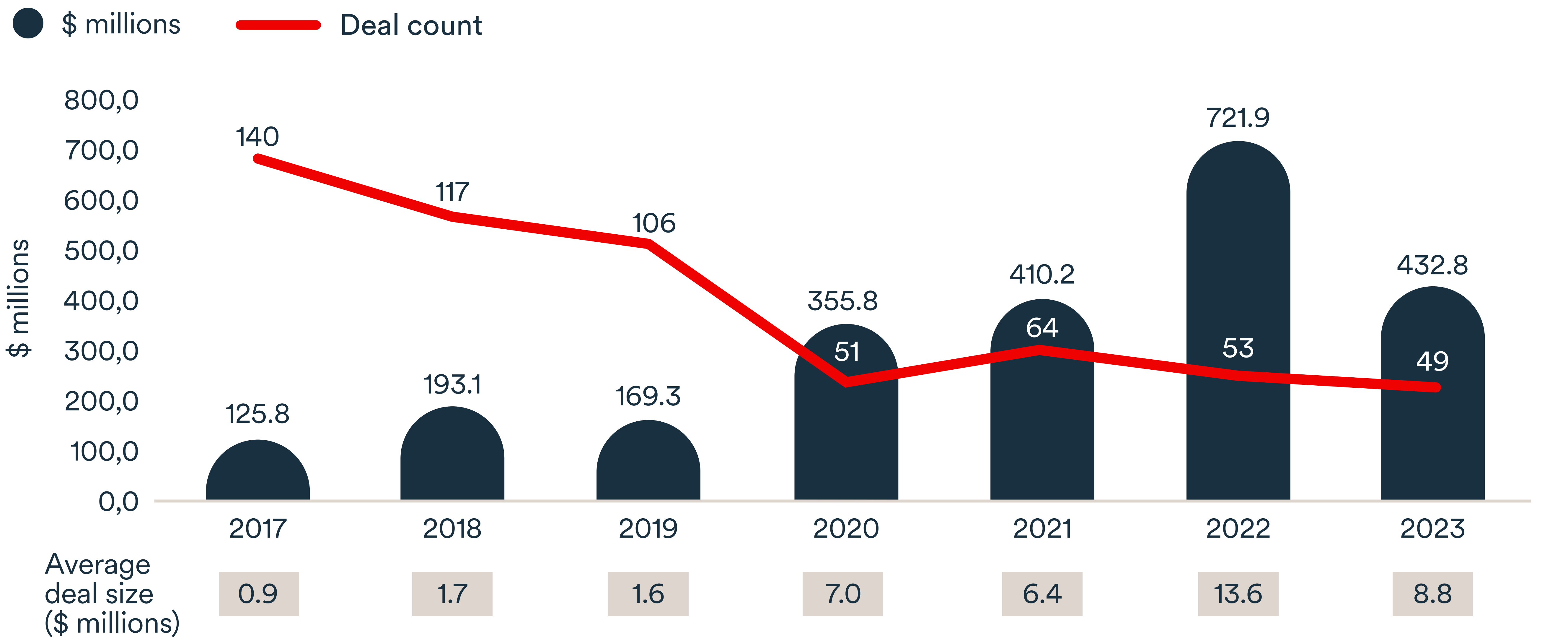


Source: BDC analysis

Venture debt losing steam after the 2022 hype

In order to extend their cash runways, companies made extensive use of venture debt in 2022—a record year for this non-dilutive capital instrument (Figure 20). The failure of the Silicon Valley Bank in 2023 left a hole in the Canadian tech-lending ecosystem, but it also prompted Canadian banks to step up and deploy additional efforts to attract start-ups. However, with interest rates at a peak, start-ups managing their cash more tightly and a general decline in venture activity, demand for venture debt decreased in 2023. As venture debt holders exhaust their liquidity, we see a potential for further equity down rounds.

Figure 20: Venture debt in Canada

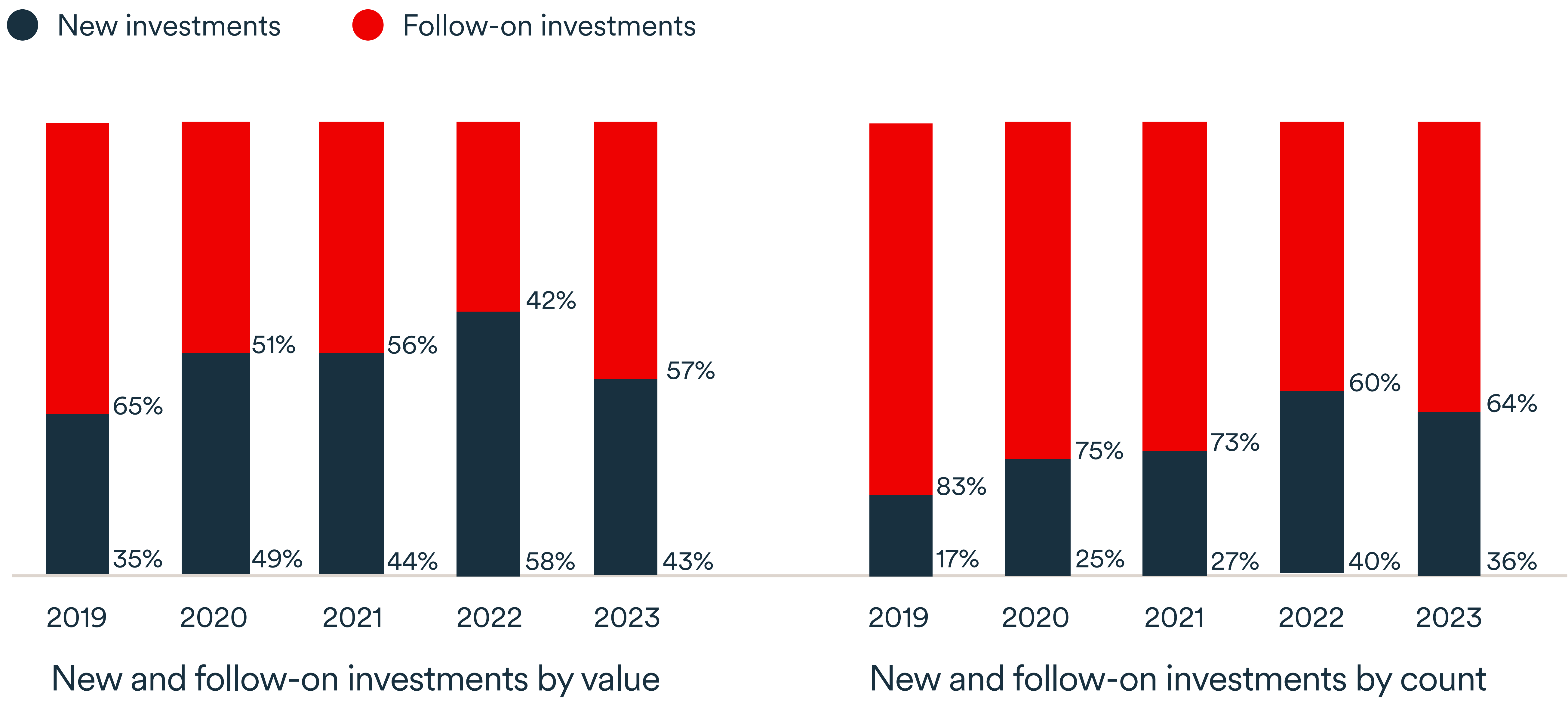


Source: CVCA, BDC analysis

Focus on internal rounds

We also observed an increased tilt towards follow-on investments in our direct portfolio in 2023, in line with the market (Figure 21). General cautiousness in deploying funds as well as weaker investment syndicates led investors to focus on optimizing their portfolio and participating in their portfolio companies' internal rounds while new activity swung towards smaller bets in seed. Seed and early-stage companies received more than 80% of dollars invested in new companies. They also accounted for a majority of the number of deals in our direct portfolio.

Figure 21: New and follow-on investments in BDC's direct portfolio



Source: BDC analysis

Higher number of down rounds

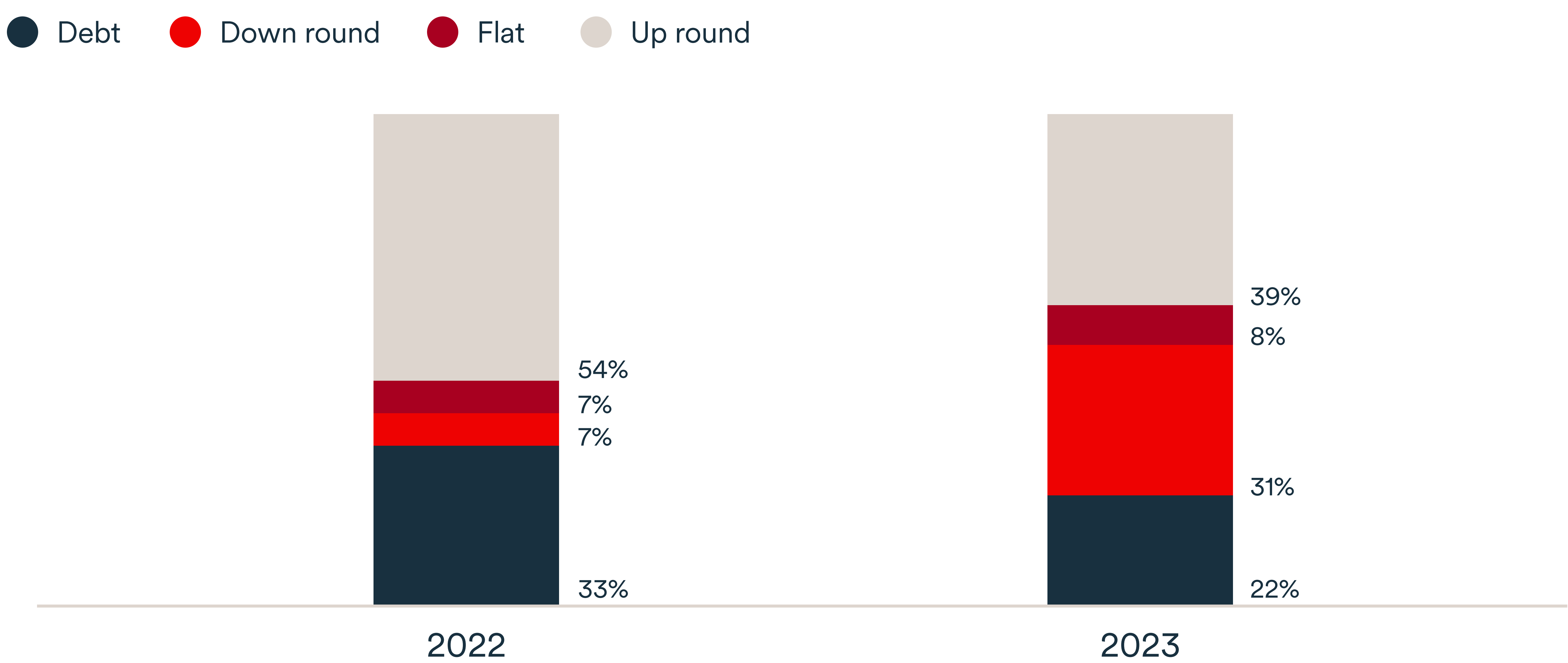
In 2023, post-money median valuations from transactions in BDC's direct portfolio decreased compared to 2022 across all stages. The number of down rounds surged from 7% in 2022 to 31% in 2023, while up rounds and convertible debt rounds contracted to 39% and 22%, respectively in 2023 (Figure 22).

The number of down rounds surged from 7% in 2022 to 31% in 2023.

Companies that are either performing well or operating within high-growth sectors, such as AI, continued to command elevated valuations and secure up rounds. As cash runways shorten and companies exhaust their bridge lines, companies will have to go back to market in order to raise a priced round and comply with investors' lower valuations.

The push and pull effect of expected interest rate cuts alongside shorter cash runways may limit further correction in valuations.

Figure 22: Investment rounds in BDC's direct portfolio by valuation status



Source: BDC analysis

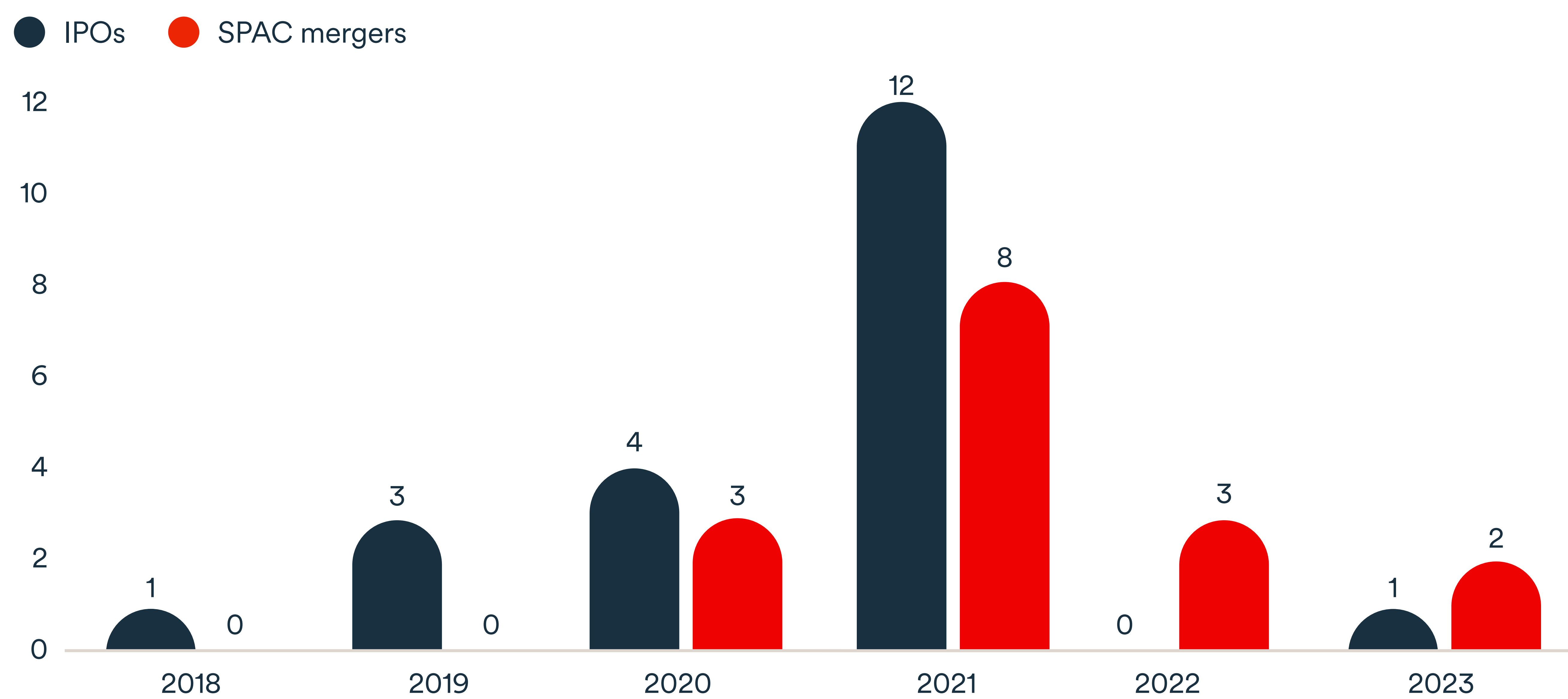
Exit activity remains under pressure

IPO lull continues, M&A exits continue

IPOs remained muted last year with only one VC-backed company making it to the public markets owing to depressed valuations and the high cost of going public. For the second consecutive year, special purpose acquisition company (SPAC) mergers have outnumbered IPOs among Canadian VC-backed companies (Figure 23).

Lately, SPACs have competed with IPOs given their speed and ability to incorporate forward-looking statements. Nevertheless, recently enacted regulations have now rendered SPACs less useful. In January 2024, approximately two years after proposing reforms for the SPAC market, the U.S. Securities and Exchange Commission has strengthened disclosure obligations for SPAC sponsors. Doing so, it aims to safeguard investors, but these requirements will increase costs and liabilities for target companies and may limit SPAC listings in the future.

Figure 23: Canadian VC-backed IPOs and SPAC mergers

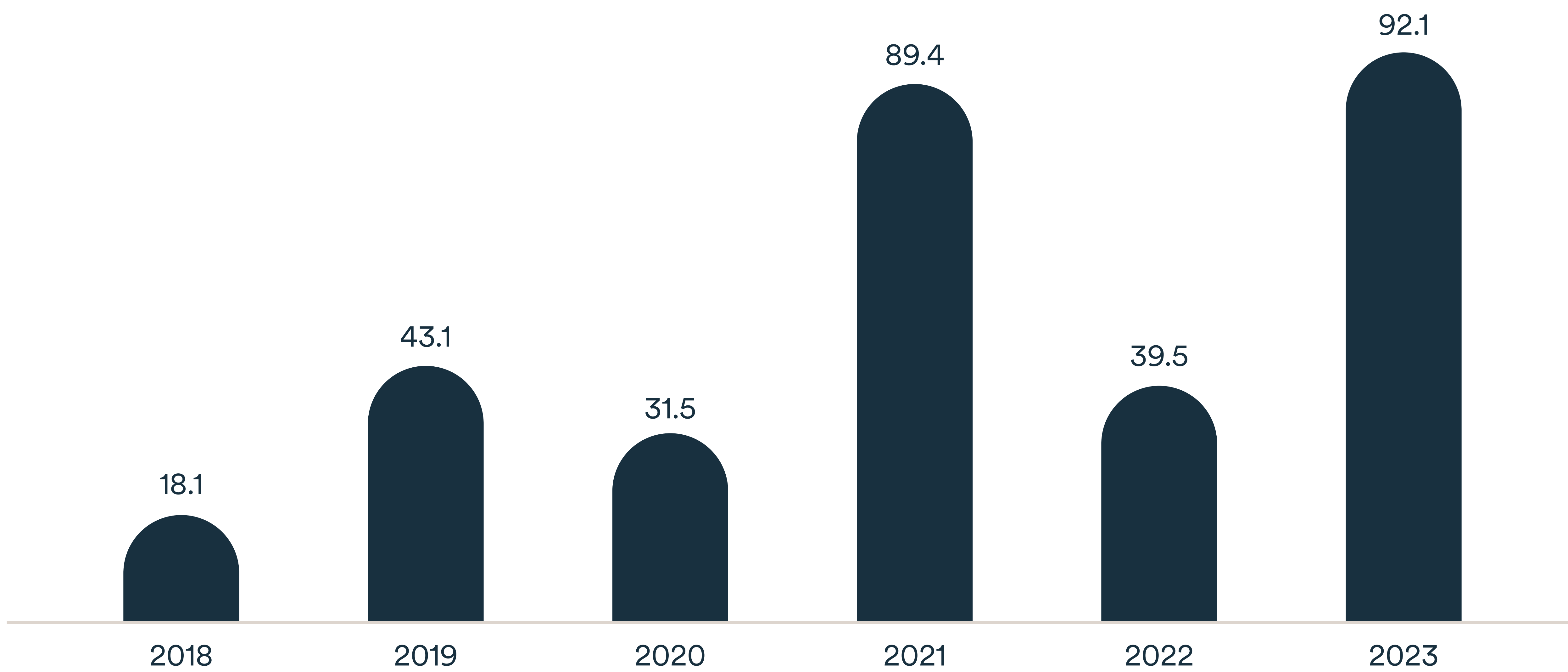


Source: PitchBook, BDC analysis

While IPO activity was weak, 2023 saw record M&A exits by value. This trend was propelled by a handful of large deals, like those involving GaN Systems, Chinook Therapeutics, Inversago Pharma and Carbon Engineering. Exit values were largely driven by acquisitions in the life sciences and ECT sectors, underscoring the momentum in these sectors.

However, with three exits of $1 billion or more last year, surpassing 2021 which had seen two deals of this size, it appears that high-quality, niche companies managed to exit despite the challenging macro environment. These high-value deals inflated the median exit value in 2023 compared to previous years (Figure 24).

Figure 24: Median exit values in Canada ($ millions)



Source: PitchBook, BDC analysis

A few large deals lead to higher exit values in Quebec and B.C.

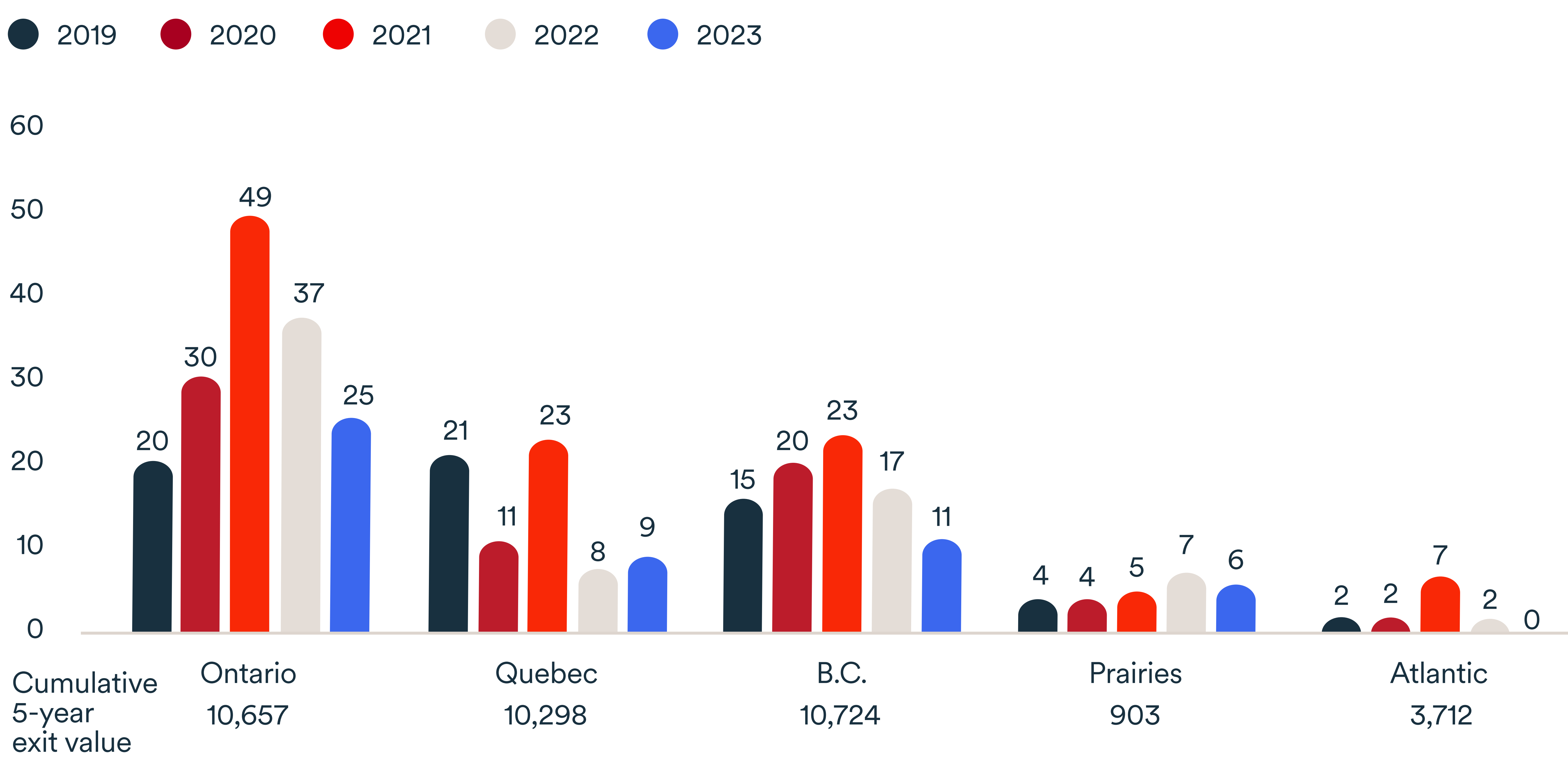
Over the last five years, the regions included in our analysis generated a total of $35 billion in exit value, with Ontario accounting for only 29% of this number despite absorbing almost half of the country's VC investments. Quebec and British Columbia contributed 28% and 30%, respectively, to total Canadian exit values, despite receiving much less of the country's VC investments. This is due to the large exits completed last year in both provinces.

The Atlantic and Prairies regions contribution to exit values is significantly smaller than others, as these regions allocate a greater proportion of capital to seed investments, which take longer to mature.

Since 2019, Quebec has showcased an ability to generate exits in excess of $50M ("mega exit"), with 32% of exits recorded achieving this threshold. Ontario is still leading in absolute terms with the highest number of mega exits over the last five years. Meanwhile, British Columbia and the Prairies recorded higher average exit values, although in the case of British Columbia, the data is skewed by the Novartis acquisition of Chinook Therapeutics for US $3.2 billion. The Atlantic and Prairies regions only generated seven of the 81 VC-backed mega exits in Canada since 2019 (Figures 25 and 26).

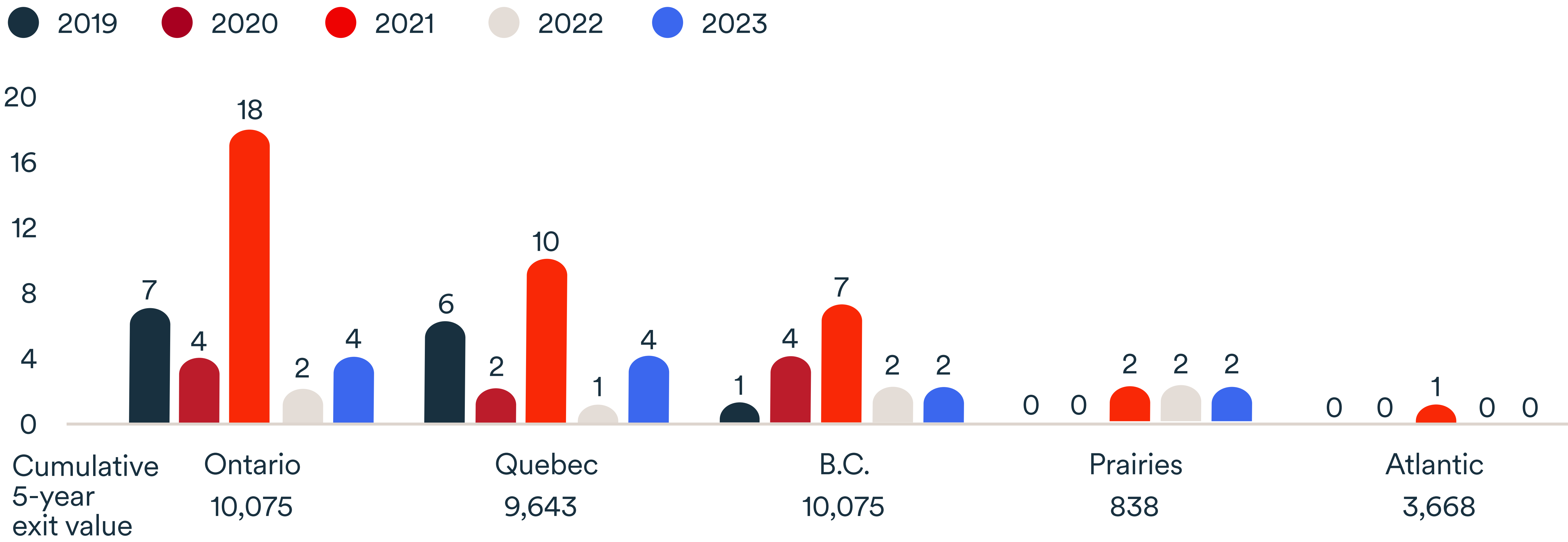
Over the last five years, the regions included in our analysis generated a total of $35 billion in exit value.

Figure 25: Regional exit count per year and total exit value ($ millions)



Source: PitchBook, BDC analysis

Figure 26: Regional exit count per year and total exit value ($ millions), exits of more than $50M

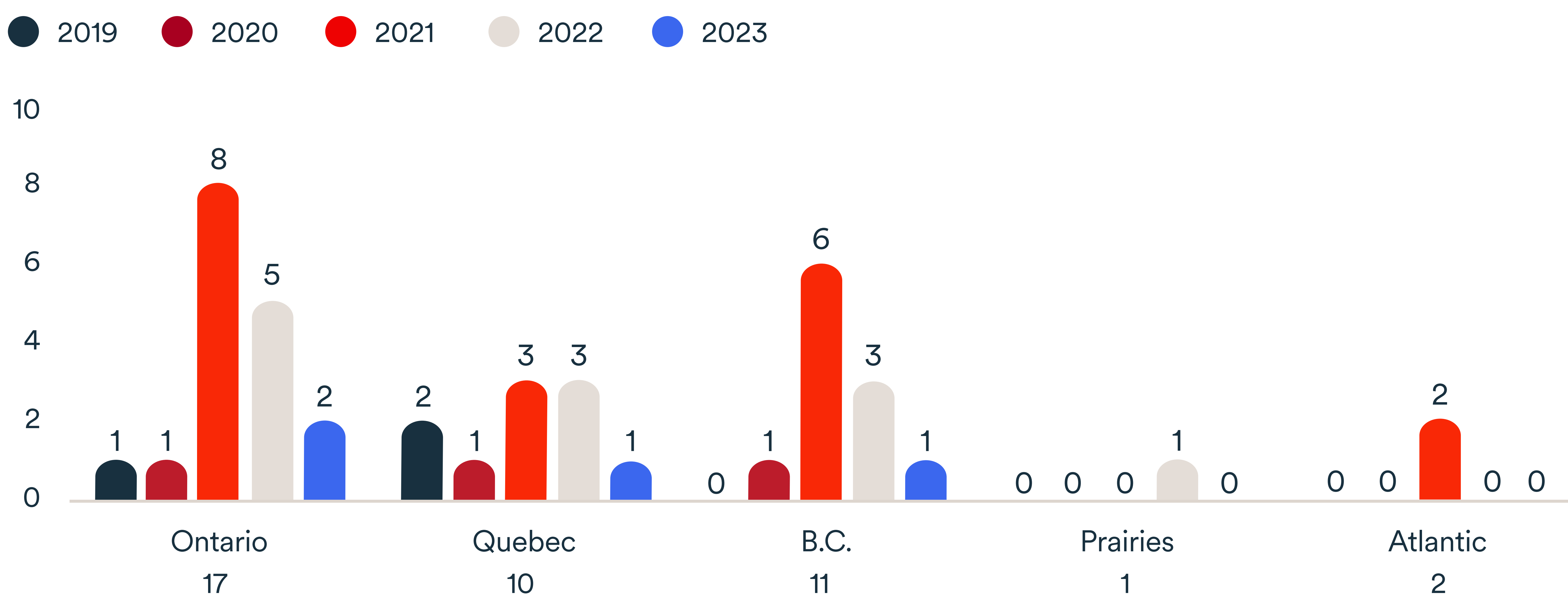


Source: PitchBook, BDC analysis

Ontario generated the highest number of unicorns

41 VC-backed unicorns were created over the last five years across Canada (Figure 27). Ontario generated the highest number of unicorns over that period, demonstrating the region's ability to grow and scale businesses. Ontario also led the way last year, with Quebec and British Columbia following not too far behind.

Figure 27: New unicorns in Canada, by region and year



Source: PitchBook, BDC analysis

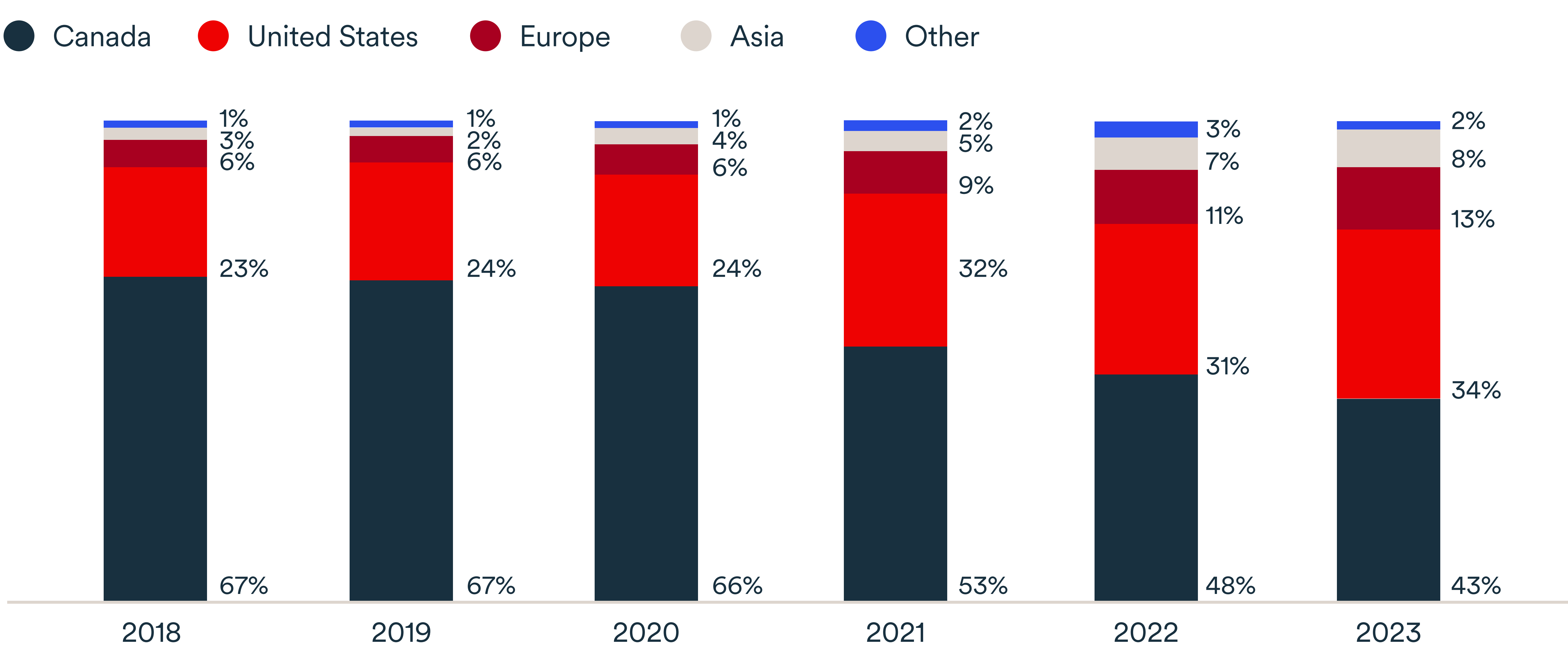
Capital availability remains adequate

Foreign participation continues to grow in Canada

The Canadian VC ecosystem continues to be a compelling opportunity for foreign investors who participated in a growing proportion of the country's deals last year (Figure 28). In 2023, close to 60% of Canadian deals saw involvement of foreign investors, a level of participation reaching peaks not witnessed in almost two decades. As such, it appears that Canadian VC remains sought after by foreign investors even during this turbulent period. In a context where overall investment has decreased, Canada's reliance on foreign investors has come into focus—a trend to be watched.

As such, it appears that Canadian VC remains sought after by foreign investors even during this turbulent period.

Figure 28: Foreign investor participation in Canadian deals, by volume

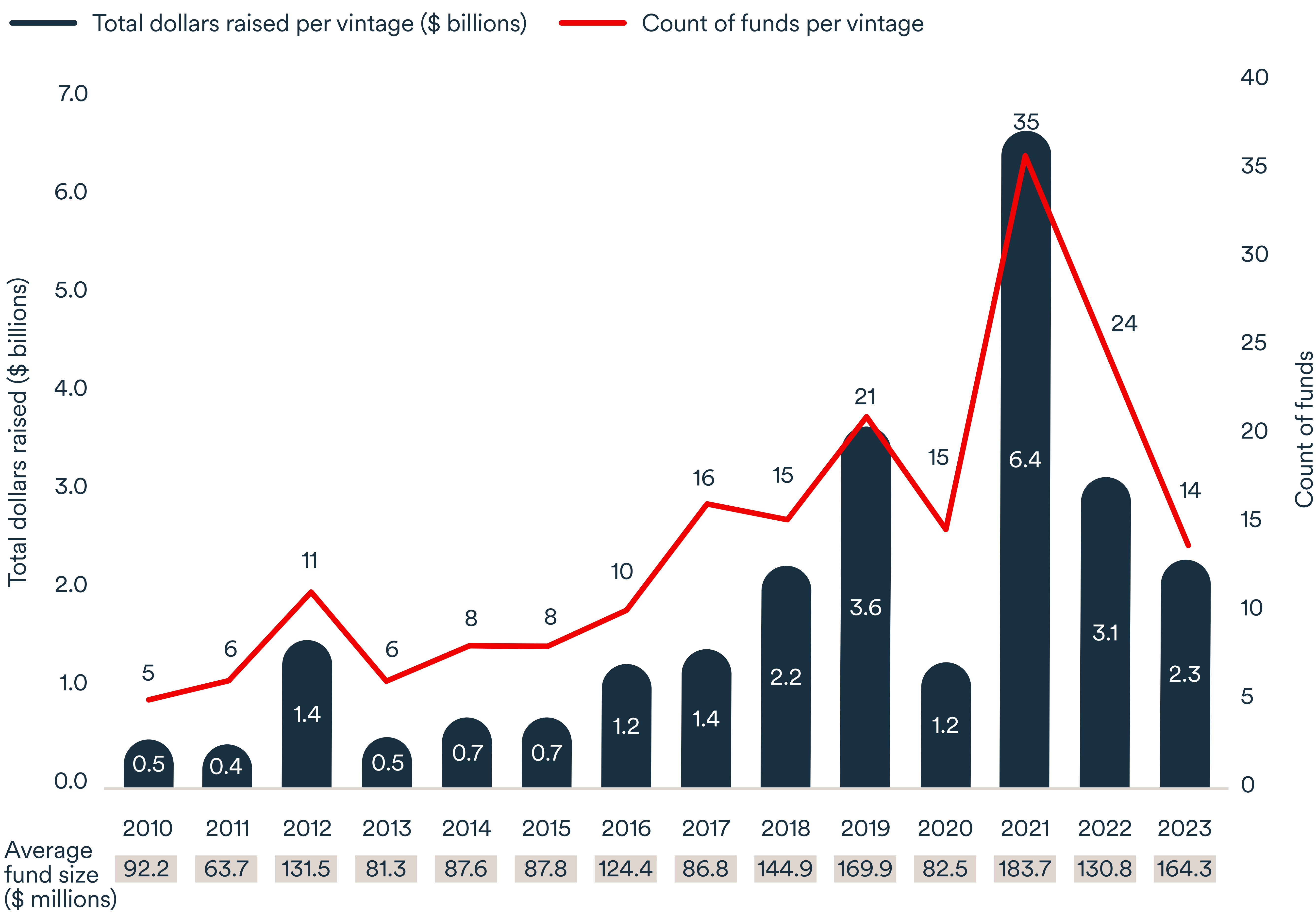


Source: Refinitiv, BDC Analysis

Fundraising activity remains higher than pre-pandemic averages

Over the 2015-19 period, a typical year would have been characterized by 14 funds each raising $130M for an average total of $1.8B per year (Figure 29). In 2023, fundraising activity declined year-over-year but remained 27% higher than the 2015-19 average annual fundraising activity. The bigger average fund size can be attributed to established managers—who are able to raise large funds despite a slow market—taking a greater share of the pie in 2023. The number of funds raised was in alignment with pre-pandemic averages.

Figure 29: Canadian VC fundraising activity



Source: BDC internal data, PitchBook, as of December 31, 2023

Note: Total dollars raised is the sum of the fund sizes of all funds in a same vintage year. We assume that the vintage of a fund is the year of its first capital call, while the fundraising could have started in the year prior.

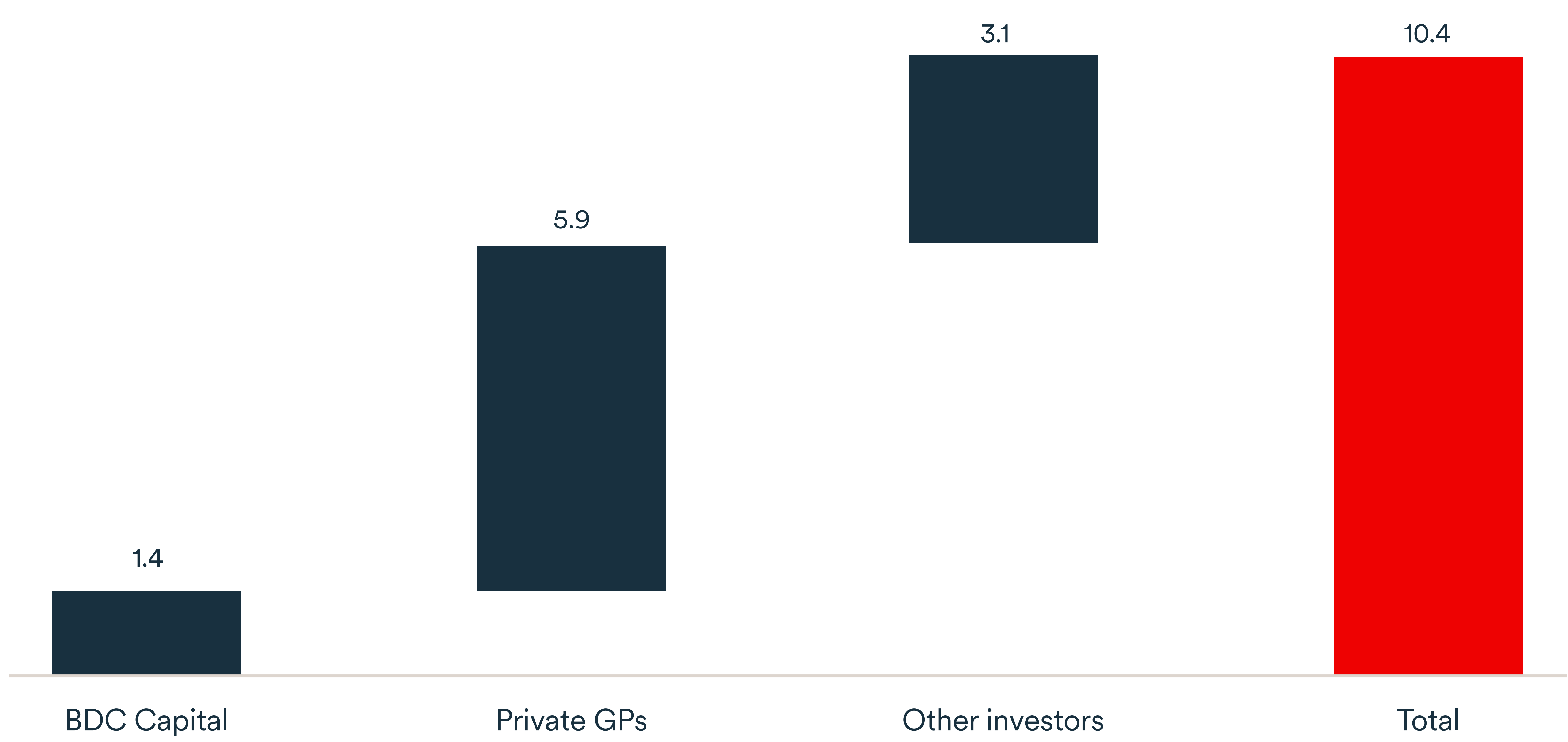
Estimated $10.4B dry powder available

We estimate that VC investors headquartered in Canada are currently sitting on $10.4 billion of dry powder, an amount inclusive of private Canadian-headquartered GPs as well as BDC, public sector VC investors and some of the most active domestic pension funds (Figure 30). Historically, 55% of Canadian investors' dry powder is deployed in Canadian companies (excluding management fees). Similarly, across the border, American VC investors currently hold $421 billion[5] in dry powder according to PitchBook. This is the highest amount in the last eight years, owing to a slowing deployment coupled with increasing contribution from new fund raises.

Historically, we estimate that the U.S. allocates on average 2% of its dry powder to Canadian companies. Record dry powder in the U.S. may trickle back to Canadian companies, potentially alleviating concerns regarding capital availability in the Canadian market over the coming years.

Historically, 55% of Canadian investors' dry powder is deployed in Canadian companies

Figure 30: Dry powder across Canadian VCs ($ billions)



Source: BDC internal data, PitchBook, as of December 31, 2023.

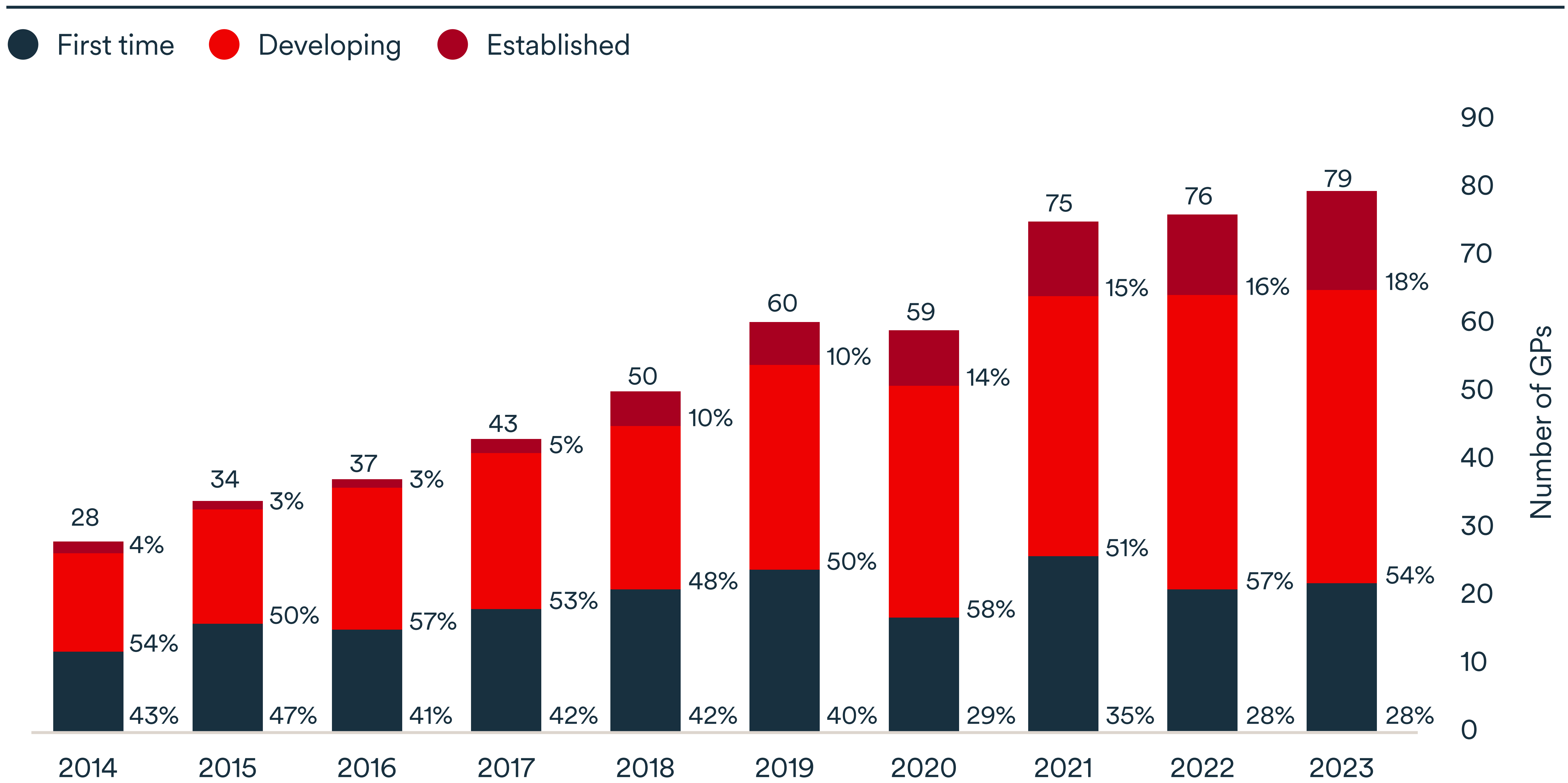
[5] PitchBook-NVCA, data as of June 30, 2023

First time and developing managers represent a significant majority of currently active GPs

The Canadian active GP landscape continues to mature as we see a progression of first-time (Fund I) and developing managers (Funds II and III) grow and successfully raise follow-on funds. As the number of active GPs increased, so has the number of managers graduating to become established managers—managers having raised a Fund IV and onward (Figure 31). The increasing number of established GPs underscores the fact that Canada is creating progressively more sustainable franchises that are able to reach an ever-growing number of LPs. However, the rate at which new GPs become active is slowing—a consequence of the headwinds arising from a challenging macro environment and factors affecting fundraising efforts—including pressure on valuations, exit environment and reallocation efforts led by institutional asset managers. Based on anecdotal observations there is a meaningful number of GPs not captured here as fundraising efforts are either still underway or abandoned altogether, not to mention managers revising first and final close targets.

Overall, we noticed that GPs are more prudent, proactive and transparent in their communication with their LPs in order to maintain sufficient trust to be successful in the fundraising of their next fund. This approach has proven especially helpful for developing GPs navigating a tough, subdued macroeconomic environment in which LPs are also facing liquidity constraints. In such a context, some managers may also right-size their targets to remain in the market and allocate more time to investing rather than fundraising.

Figure 31: Active GPs, by maturity



Source: BDC internal data, PitchBook

Data includes Canadian private independent VC funds that closed with a fund size of $10M or more. Excludes PE funds, private debt, funds of funds, government funds and accelerators. It also excludes GPs where the most recent fund vintage is older than five years.

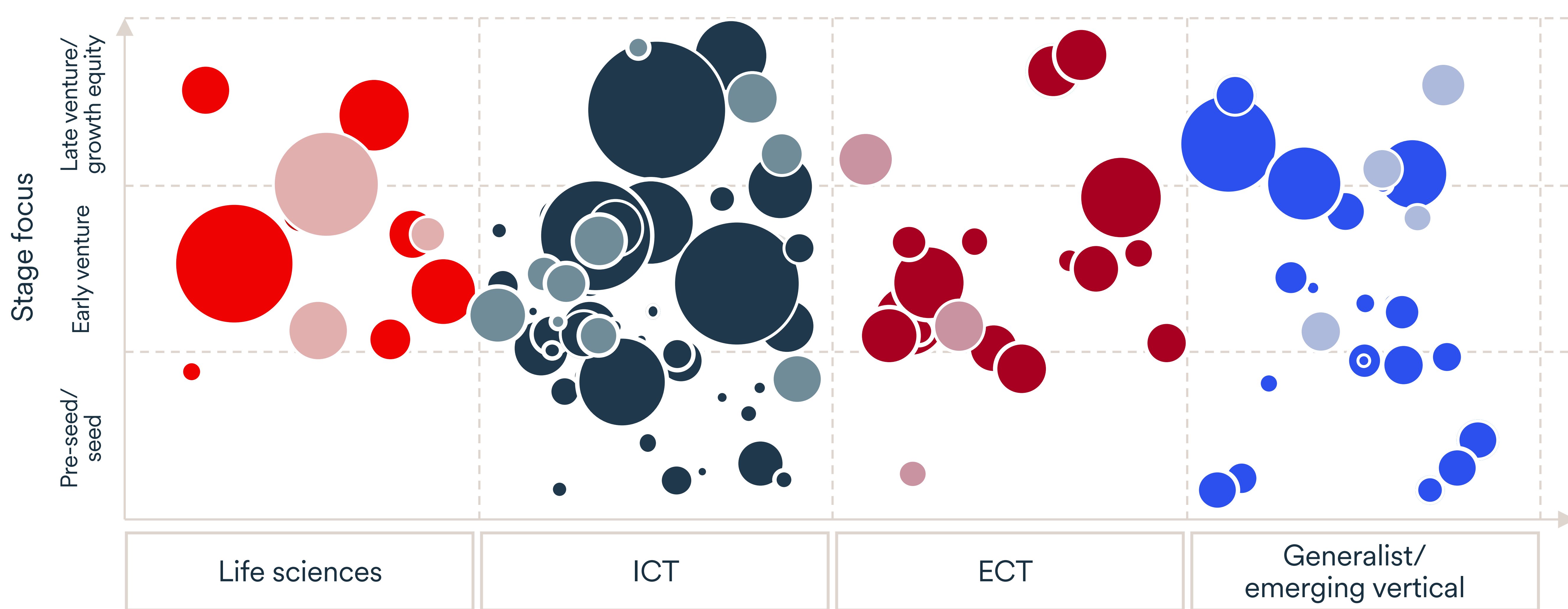
Greater LP caution; continued dearth of GPs in life sciences and ECT

Macroeconomic headwinds have led to greater LP caution, slower deployment of capital by GPs and a general decline in fund activity from the peak seen in 2021. The heightened diligence and caution exerted by LPs can promote discipline and improved standards amongst GPs, which trickles down to the value proposition GPs will expect from entrepreneurs.

Looking at GP presence by stage and sector, our analysis reveals that we continue to see gaps in the number of active private funds across the life sciences sector, in the pre-seed, seed, late venture and growth equity stages. This limits both pipeline development as well the emergence of Canadian champions (Figure 32).

Gaps have also appeared in the ECT sector, creating opportunities in similar stages as the life sciences sector. It is worth noting that we are increasingly seeing generalist GPs trying to address climate change by investing in capital-light ECT companies, but this is still not enough to bridge the eventual need in the market. For Canada to succeed in its transition to a clean economy, increased fund activity in this sector is therefore imperative. To reach net zero emissions by 2050, Canada would require average investments ranging from $60 billion to $140 billion every year leading up to that date.

Figure 32: GP presence, by stage and sector



Source: BDC internal data, PitchBook. Data include Canadian private independent VC funds that closed with a fund size of $10M or more and BDC Capital direct funds. Excludes PE funds, private debt, funds of funds, government funds and accelerators. Graphic presents only the most recent fund for each respective GP that is no older than 12 years (2011 vintage).

Bubble size represents actual/target fund size—not all capital may be deployed in Canada. Bright colors are active funds that are no older than five years. Faded colors are active funds that are 6-12 years old.

Future ecosystem growth threatened by fragile underpinnings

After seeing VC activity come down from record levels in 2021 and witnessing interest rates reach new highs in 2023, the Canadian VC community was understandably feeling bleak last year. The numbers reported here, while not grim, underscore the ecosystem's vulnerability.

As we saw, VC activity appears to be closer to the levels of the 2015-19 era, with Canadian VC investments declining more slowly compared to global trends—showing some relative resilience. While late and growth equity stage investments were both hit particularly hard last year, we must also recognize that Canada is not an outlier; cutting back on investments was the prevailing tendency among late-stage investors, whether in Canada or abroad. We note that should this late-stage gap in capital persists, early-stage companies may lack funding as they look to scale over time.

Looking to the year ahead, we see risks to the industry should valuations continue to stagnate or drop further, causing long-term returns to dip into single digit territory. Should this materialize, it could compel institutional investors to stray further from their designated portfolio allocations for VC investments, potentially impacting capital availability in the ecosystem.

Hopefully, we are simply returning to a point of sustainable growth. For example, M&A activity could see an uptick if interest cuts materialize as anticipated. Expected lower cost of capital could also sustain fundraising activity, allowing for activity levels to remain comparable to those seen in 2023.

Canadian entrepreneurs may be able to attract comparatively more investor support this year, but given the increased focus of GPs on follow-on investments in 2023, previously backed quality start-ups may find it easier.

BDC is committed to upholding its role as a key player in Canada's VC ecosystem. For instance, we believe the recent launch of the $50 million Seed Venture Fund will help alleviate capital availability at the earliest stages of development and foster a robust investment pipeline of early stages companies for the next decade. We will also increase our support for the late and growth stages that suffered from investor retrenchment.

Our aspiration is that these efforts, combined with those of other key actors across the country, will help empower entrepreneurs and propel the Canadian VC industry forward, thereby laying the groundwork for a prosperous 2024 and beyond.

BDC is by your side every step of the way

Learn more about our different funds and our support for the Canadian venture capital ecosystem.

For more information

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